United States Court of Appeals

for the Second Circuit

APPENDIX

74-2405

In The

United States Court of Appeals

For The Second Circuit

GERALD L. HERZFELD,

Plaintiff-Appellee,

- against -

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendant-Appellant.

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Third-Party Plaintiff-Appellee,

- against -

ALLEN & COMPANY, INCORPORATED and ALLEN & COMPANY,

Third-Party Defendants-Appellants.

ALLEN & COMPANY and ALLEN & COMPANY INCORPORATED,

Third-Party Counterclaimants-Appellants,

- against -

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Third-Party Counterclaim Respondent-Appellee.

JOINT APPENDIX

Volume I, pp. 1a – 300a

BLUM, HAIMOFF, GERSEN, LIPSON & SZABAD
Attorneys for Appellee Gerald L. Herzfeld
270 Madison Avenue
New York, New York 10016
683-6383

WILLKIE, FARR & GALLAGHER
Attorneys for Appellant and Appellee Laventhol, Krekstein, Horwath & Horwath
1 Chase Manhattan Plaza
New York, New York 10005
248-1000

POLLACK & SINGER
Attorneys for Appellants and Appellees Allen & Company, Inc. and Allen & Company
61 Broadway
New York, New York 10006
952-0330

UNITED STATES COURT OF APPEALS
FILED
DEC 24 1974
A. DANIEL FUSARO, CLERK
SECOND CIRCUIT

(7910) LUTZ APPELLATE PRINTERS, INC.
Law and Financial Printing

South River, N. J. (201) 257-6850 | New York, N. Y. (212) 565-6377 | Philadelphia, Pa. (215) 563-5587 | Washington, D. C. (202) 783-7288

B

8

PAGINATION AS IN ORIGINAL COPY

TABLE OF CONTENTS

	Page
Certified Copy of Docket Entries	1a
Summons Filed May 18, 1971	8a
Complaint Filed May 18, 1971	10a
Answer of Defendant Laventhol, Krekstein, Horwath and Horwath Filed July 23, 1971 .	42a
Answer of Defendants Allen & Co., Inc.; Allen & Co.; Charles Allen; Lee W. Meyer & Irwin H. Kramer, Filed July 30, 1971	55a
Stipulation and Order Dismissing Action on Merits with Prejudice and Costs Against all Defendants Except Laventhol, Krekstein, Horwath & Horwath -- Memorandum Endorsed on Stipulation Setting Stipulation Aside Filed November 24, 1971	62a
Notice of Settlement With Memorandum Endorsed Approving Settlement and Dismissal and Permitting the Bringing of Third-Party Action Filed December 13, 1971	66a
Affidavit of Defendants Allen & Co., Inc. Allen & Co,; Charles Allen; Lee W. Meyer and Irwin H. Kramer in Support of Dismissal Filed December 15, 1971 . .	72a

Contents

	Page
Exhibit A - Letter Annexed to Foregoing Affidavit	86a
Exhibit B - Letter Annexed to Foregoing Affidavit	87a
Affidavit of Attorney for Defendant Laventhol in Opposition to Dismissal Filed December 15, 1971	88a
Memorandum of Defendant Allen and Co., Inc.; Allen & Co.; Charles Allen; Lee W. Meyer and Irwin H. Kramer in Support of Dismissal Filed December 15, 1971	95a
Amended Complaint Filed December 30, 1971	105a
Answer of Defendant Filed January 24, 1972	117a
Report Dated December 6, 1969 Annexed to Foregoing Answer	124a
Financial Statements Annexed to Foregoing Answer	125a
Notes to Financial Statements Annexed to Foregoing Answer	127a
Third-Party Complaint Filed January 31, 1972	131a

Contents

	Page
Answers and Counterclaims of Third-Party Defendants the Firestone Group, Ltd.; Allen & Co., Inc.; Allen & Co,; Charles Allen; Lee W. Meyer and Irwin H. Kramer Filed February 29, 1972 . .	144a
Reply of Defendant/Third-Party Plaintiff Laventhol to Counterclaim of Third-Party Defendants Filed March 21, 1972 .	160a
Report Dated December 6, 1969 Annexed to Foregoing Reply	169a
Financial Statements Annexed to Foregoing Reply	170a
Notes to Financial Statements Annexed to Foregoing Reply	172a
Opinion No. 40,745 Filed May 29, 1974 . .	176a
Affidavit of Defendant/Third Party Plaintiff Laventhol in Opposition to Motion to Amend Judgment of Third-Party Defendants Filed June 14, 1974	250a
Judgment and Order No. 74,498 Filed June 13, 1974	256a
Pre-Trial Order of Plaintiff Filed June 5, 1974	259a

Contents

	Page
Trial Transcript Dated October 15, 1973 . .	266a
Trial Transcript Dated October 16, 1973 .	266a-30
Trial Transcript Dated October 18, 1973 . .	267a
Trial Transcript Dated October 19, 1973 . .	440a
Trial Transcript Dated October 23, 1973 . .	628a
Trial Transcript Dated October 25, 1973 . .	646a
Trial Transcript Dated October 29, 1973 . .	964a
Reply Affidavit of Allen and Co., Inc. and Allen and Co. In Support of Motion to Amend Findings and Judgment Filed September 13, 1974	1067a
Notice of Motion of Plaintiff to Amend Findings of Fact and Conclusions of Law -- Memorandum Endorsement on Motion Filed September 13, 1974	1071a
Affidavit of Louis Haimoff in Support of Motion Filed September 13, 1974	1073a
Affidavit of Allen and Co., Inc. and Allen and Co. in Support of Motion Filed September 13, 1974	1080a

Contents

	Page
Affidavit of Daniel A. Pollack in Support of Motion	1082a
Decision No. 41169 Filed September 13, 1974	1086a
Amended Judgment No. 74,800 and Order Filed October 8, 1974	1099a
Notice of Appeal of Allen and Co., Inc. and Allen and Co. Filed October 18, 1974	1102a
Notice of Appeal of Laventhol Filed November 6, 1974	1104a
Stipulation Submitting True Copy Filed November 25, 1974	1106a
Defendant Laventhol's Memorandum of Law Annexed to Foregoing Stipulation Filed December 15, 1974	1108a
Certificate of Clerk Filed December 18, 1974	1116a

Witnesses

Gerald L. Herzfeld:	
Direct	266a-33, 273a
Cross	284a
Redirect	352a

Contents

	Page
Leonard H. Fell:	
Direct	358a
Cross	379a, 441a
David G. Baird:	
Direct	418a
Cross	419a
Chester P. Wadley:	
Direct	518a
Cross	535a, 574a
Redirect	587a
Recross	591a
Martin A. Scott:	
Direct	546a
Cross	556a
Recross	572a
Sam Winograd:	
Direct	594a
Cross	599a
Arnold L. Lipkin:	
Direct	602a, 677a, 906a
Cross	949a
George M. Duff, Jr.:	
Direct	635a
Cross	658a

Contents

	Page
Maurice Goodman:	
Direct	685a
Cross	688a
Lee W. Meyer:	
Direct	694a
Cross	699a
Richard M. Firestone:	
Direct	762a
Cross	808a
Redirect	814a
Recross	815a
Eli Boyer:	
Direct	816a
Cross	830a
Charles Chazen:	
Direct	835a
Cross	872a
Robert Feinberg:	
Direct	968a

Contents

Page

Plaintiff's Exhibits:

1 — Letter from David G. Baird to Messrs. Herzfeld E1

2 — Letter from Richard M. Firestone to Gerald Herzfeld Dated November 21, 1969 . . . . . E5

3 — Note and Stock Purchase Agreement Dated November 10, 1969 . . . . . E7

4 — Telegram Dated December 10, 1969 . . . . . E24

5A — Check in Amount of $255,000.00 Dated December 15, 1969 . . . . . E25

5B — Check in Amount of $255,000.00 Dated December 15, 1969 . . . . . E27

6 — Letter From R. L. Firestone to Gerald L. Herzfeld Dated December 16, 1969 . . . . . E28

7 — CPA Report of the Firestone Group Ltd. From December 6, 1968 to November 30, 1969 . . . . . E31

Contents

	Page
8 — Cover Letter to Purchasers of the Firestone Group Ltd. Dated December 16, 1969	E40
8A — Certification of Richard M. Firestone Dated December 16, 1969	E42
9 — Annual Report to Shareholders - 1970.	E43
10 — Releases	E61
11 — Time Report	E106
12 — Audit Review Questionnaire	E108
13 — Weekly Work Sheet	E113
14 — General Journal	E115
15 — Purchase and Sale Sheets Re: Monterey Nursing Home	E116
16 — Balance Sheets	E126
17 — Memorandum Dated November 21, 1969	E137
18 — Additional Entry Sheets	E139
19 — Note	E141

Contents

	Page
20 — Memorandum	E142
21 — Agreement Dated November 26, 1969	E144
22 — Agreement Dated November 22, 1969	E149
23 — Notes Dated November 30, 1969 . .	E155
24 — List of Employees	E156
25 — Memorandum	E157
26 — Letter from Rochelle Securities Corp. Dated December 15, 1969	E158
27 — Letter from General Investors Co. Dated December 11, 1969	E159
28A — Letter from Rochelle Securities Corp. Dated December 15, 1969 . . .	E160
28B — Check in Amount of $255,000.00 Dated December 15, 1969	E161
29A — Letter from N.E. Herzfeld Dated December 15, 1969	E162
29B — Promissory Note	E163

Contents

	Page
30 — Check in Amount of $85,000.00 Dated December 15, 1969	E164
31 — Letter From Jacobs, Persinger and Parker Dated December 16, 1969 .	E165
32 — Letter From Richard M. Firestone Dated November 12, 1969	E171
33 — Certification of Richard M. Firestone Dated December 16, 1969	E173
34 — Notice to Creditors	E174
35 — Notice	E176
36 — Proof of Claim	E177
37A — Bank Confirmations and Cutoff . .	E181
37B — Request For Confirmation	E212
38 — Notes	E238
39 — Notes	E239
Defendant's Exhibits:	
A — Deposition of Gerald L. Herzfeld . .	E240
C — Letter From Morris A. Schwalb to Chester Wadley Dated November 17, 1969	E345

Contents

	Page
D — Letter From the Firestone Group, Ltd. to Laventhol, Krekstein, Horwath & Horwath	E347
E — Letter From the Firestone Group, Ltd. to Laventhol, Krekstein, Horwath & Horwath Dated May 26, 1970	E348
F — Letter From Morris A. Schwalb to Chester Wadley Dated November 17, 1969	E350
G — Minutes of Meeting Held November 13, 1969	E352
H — Releases	E357
I — Bi-Weekly Time Report	E369
J — Bi-Weekly Time Report	E371
Third Party Defendant Exhibits:	
A-1 — Agreement Dated November 22, 1969	E375
A-2 — Agreement Dated November 26, 1969	E381
A-3 — Memorandum Dated December 2, 1969	E386

Contents

	Page
A-4 — Balance Sheets From December 26, 1968 to November 30, 1969	E388
A-5 — C.P.A. Report	E396
A-6 — Agreement Dated November 26, 1969	E403
A-9 — Laventhal Consolidated Work Paper	E404
A-10 — Laventhal Work Papers	E407
A-11 — Additional Adjusting Entries . .	E418
A-13 — Laventhal Work Papers Headed "Other Deferments"	E421
A-14 — Letter From Morris Schwalb to Chester Wadley Dated December 18, 1969	E422
A-16 — Notes	E423
A-17 — Balance Sheet	E424
A-19 — General Journal	E425
A-20 — Audit Review Questionnaire . . .	E445

Contents

	Page
A-22 — Letter From Eliot Hyman to Allen & Co. Dated February 25, 1971 .	E450
A-23 — Letter From Maurice Goodway to Allen & Co. Dated October 23, 1973	E458
A-24 — Order	E461
A-26 — S.E.C. Bulletin	E463
A-27 — Accounting For Retail Land Sales	E467

CERTIFIED COPY OF DOCKET ENTRIES

CIVIL DOCKET
UNITED STATES DISTRICT COURT

JUDGE MAC MAHON 71 CIV. 220

TITLE OF CASE	ATTORNEYS
LD L. HERZFELD, Plaintiff, v. FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, W. MEYERS, IRWIN H. KRAMER, RICHARD M. STONE, MARTIN A. SCOTT, HOFFMANN, WISE & SHEPARD, JAMES W. DEER, JACOBS, PERSINGER & PARKER, and LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, 11/5/71 Defendants.	For plaintiff: Blum Haimoff Gersen Lipson & Szabad 270 Madison Ave. NY 10016
	For defendant: Willkie Farr & Gallagher (for Laventhol Krekstein Horwath & Horwath) One Chase Manhattan Plaza NY 10005 L22-3100 Holtzmann, Wise & Shepard (for James W. Deer and James W. Deer) 30 Broad St. NY 10004 HA 2-7740 Pollack & Singer (for Allen & Co., Inc. Allen & Co., Charles Allen, Lee W. Meyers and Irwin H. Kramer) 111 Broadway NY 10006 WO 4-5770 D'Amato, Costello & Shea (for [illegible] Persinger & Parker) 116 John St. [illegible] Lipper, Keeley, Katcher, Lowey & Lamb (for [illegible] and Wolkowitz & Peckman) (for Martin A. Scott) 11 East 42nd St. NY 10017 MU 2-5710 Martin A. Scott, pro se, no address given.

DATE	PROCEEDINGS
11/5/71	Filed Complaint & issued summons
	ALLEN & COMPANY, INCORPORATED
	ALLEN & COMPANY
	CHARLES ALLEN
	LEE W. MEYERS
	IRWIN H. KRAMER
	RICHARD M. STONE
	MARTIN A. SCOTT
	DAVID REID 3rd Pty. Defts.

STATISTICAL RECORD	COSTS	DATE	NAME OF RECEIPT NO.	REC.	DISB.
J.S. 5 mailed X	Clerk	5/17	Allen & C.	15	
J.S. 6 mailed ✓	Marshal	5/21	Allen		15
Basis of Action: ICL.S.E.C. ACT 1933 §4	Docket fee				
$1,510,000	Witness fees				
Action arose at:	Depositions				

A

NOV 29 1971

2a

JUDGE MAC MAHON 71 CIV. 2209

	PROCEEDINGS	Date Order or Judgment
May13-71	Filed Complaint. Issued Summons.	
May18-71	Filed Notic of Assignment. J. Palmieri	
Jun 9-71	Filed stipulation and order extending deft. Laventhol Krekstein Horwath & Horwath's time to answer complaint to 7/9/71. So ordered. Palmieri, J.	
Jun. 11-71	Filed stip and order that the time for defts' Jacobs, Persinger & Parker, to answer complaint is ext. from 6-10-71 to 7-8-71. So Ordered; Palmieri, J.	
Jun 23-71	Filed stipulation and order extending defts. Allen & Co.Inc., Allen & Co., Charles Allen, Lee W. Meyers, Irwin H. Kramer, Holtzmann, Wise & Shepard and James W. Deer's time to answer complaint to 7/8/71. So ordered. Palmieri, J.	
Jul 7-71	Filed stipulation and order extending deft. Laventhol Krekstein Horwath & Horwath's time to answer complaint to 7/23/71. So ordered. Palmieri, J.	
Jul.13-71	Filed Summons with Marshal's ret. Served. Lee W. Meyers, by Mr. Chini on 5-21-71 Served Charles Allen, by Mr. Chin on 5-21-71 Served Allen & Co. by Mr. Chin on 5-21-71 Served Irwin H. Kramer, C/O Allen & Co. by Mr Chin on 5-21-71 Served Firestone, Ltd. by Martin A. Scott on 5-25-71 Served Richard M. Firestone C/O Firestone Ltd. by personally on 5-25-71 Served Martin A. Scott, C/O Firestone Ltd. by personally on 5-25-71 Served Holtzmann Wise & Sheppard, by Mr. Chin on 5-21-71 Served James W. Deer C/O Holtzmen, Wise & Shapiro, by Mr. Chin on 5-21-71 Served Jacobs Persinger & Parker by Mr. H. Robert Finsberg, on 5-21-71 Served Laventhol, Krekstein, Horwath & horwath, by Mr. Chin on 5-21-71	
Jul 21-71	Filed stipulation and order extending defts. Allen & Co.Inc., Allen & Co., Charles Allen, Lee W. Meyers, Irwin H. Kramer, Holtzmann, Wise & Shepard and James W. Deer's time toanswer complaint to 7/15/71. So ordered. Palmieri, J.	
Jul 23-71	Filed Notice of Deposition. of Plaintiff.	
Jul 23-71	Filed ANSWER ofdeft. Laventhol, Krekst in, Horwath & Horwath to complaint.	WF&C
Jul 27-71	Filed stipulation and order extending defts. Allen & Co.Inc., Allen & Co., Charles Allen, Lee W. Meyers and Irwin H.Kramer's time to answer complaint to 7/29/71. So ordered. Palmieri, J.	
Jul 30-71	Filed ANSWER of Holtzmann, Wise & Shepard and James W. Deer to complaint.	H,W&S
Jul 30-71	Filed Notice of Examination of Plaintiff Gerald L. Herzfeld.	
Jul 30-71	Filed First Set of Interrogatories propounded by defts. Allen & Co.,etc.	
Jul 30-71	Filed ANSWER of defts. Allen & Co.Inc., Allen & Co., Charles Allen, Lee W.Meyers and Irwin H. Kramer.	
Aug.2-71	Filed pltff's notice to take deposition of deft. Jacobs, Persinger & Parker, on 8-16-71.	P&S
Aug. 2-71	Filed pltff's Notice to Take Deposition of deft. Charles Allen, on 8-11-71, etc.	
Aug.12-71	Filed Notice of Deposition of Plaintiff.	
Aug.12-71	Filed ANSWER of defts. Jacobs Persinger & Parker to complaint.	DC&S
Aug.16-71	Filed Notice of Depositions.	
Aug.31-71	Filed stip and order that the time for deft. Martin A. Scott, to answer complaint is ext. to 9-15-71. So Ordered; Palmieri, J.	
Sep.15-71	Filed stip and order that the time for deft. Richard M. Firestone, to answe complaint is ext. to 9-15-71. So Ordered; Tyler, J.	
Sep 17 71	Filed deft's Richard M. Firestone, notice of motion Re: Dismiss. Ret. 10-26-71	
Sep 17 71	Filed Memorandum of law in support of motion to dismiss.	

Chief Mag. Judge

B

HERLFELD

JUDGE PALMIERI

Civil Docket Continuation

JUDGE MAC MAHON [illegible] JUDGE PALMIERI

	PROCEEDINGS	Date Ord. Judgment
Sep.23-71	Filed pltff's Notice to take Deposition of deft. Martin A. Scott, on 10-20-71.	
Sep.23-71	Filed defts' Charles Allen, Allen & Co., Allen & Co., Inc. Lee W. Meyers and Irwin H. Kramer, Notice for Production of Documents.	
Sep.24-71	Filed defts' Allen & Co. Inc. Allen & Co., Charles Allen, Lee W. Meyers and Irwin H. Kramer, First Request for Production of Documents	
Sep.24-71	Filed deft. Jacobs, Persinger & Parker's Request for Production of Documents	
Oct.1-71	Filed ANSWER of Martin A. Scott to complaint.	
Oct.7-71	Filed stip and order that the time for deft. Martin A. Scott, to answer complaint is ext. from 9-15-71 to 10-4-71. Edelstein, J.	LKE
Oct.13-71	Filed stipulation and order that active participation by the deft. Richard M. Firestone in pretrial discovery shall not be construed or deemed to constitute a waiver of the defendant's right to quashservice of process or seek a dismissal of the complaint due to insufficiency of service of process. So ordered. Palmieri, J.	
Nov.5-71	Filed stipulation and order discontinuing action on the merits, withprejudice and without costs as against all defts. except Laventhol, Krekstein, Horwath & Horwath, etc. So ordered. Palmieri, J.	
Nov.24-71	Filed Memo Endorsed on Stipulation filed 11-5-71--Of the Court of 11-3-71 order, set aside because counsel for the deft. Laventhol, Krekstein and Horwath & Horwath was not sign the stipulation or given notice that such stipulation would be submitted to the Court Sec. Rule 41 FRCP. Palmieri, J. M/N	
Dec.13-71	Filed Notice of Settlement Palmieri, J. with Memo Endorsed filed this date--This settlement between the pltff. and all the defts' except the Laventhol firm, is hereby approved after argument. Since counsel agree that an amended complaint, which Mr. Haimoff, counsel for pltff. expects to serve within 20 days, will set in motion the procedural steps whereby the deft. Laventhol, if it is so advised, can bring 3rd party actions against any of the settling defts'., there is no unfairness to the objectiong deft. Laventhol. Palmieri, J. M/N	
Dec.15-71	Filed Affidavit in support of dismissal.	
Dec.15-71	Filed Affidavit of Attorney for Richard M. Firestone.	
Dec.15-71	Filed Affidavit of Louis A. Draco.	
Dec.15-71	Filed Memorandum in support of Dismissal.	
Dec.15-71	Filed affidavit of Stephen Lowey.	
Dec.15-71	Filed Deft. Laventhol Krekstein, Howath & Howath's Memorandum of Law in opposition to proposed settlement by other defendants and in support of terms and conditions of such settlement.	
Dec.15-71	Filed Affidavit of Louis Haimoff.	
Dec.15-71	Filed Affidavit of Richard G. McGahren. In support of request that stip. be "So ordered".	
Dec.15-71	Filed Affidavit of Frank P. Brot.	
Dec.30-71	Filed AMENDED COMPLAINT.	
Jan 13/72	Filed Stip. & Order extending time to answer to 1/21/72	
Jan.24-72	Filed ANSWER of deft to amended complaint.	WF&G
Jan.31-72	Filed third-party complaint and issued 3rd pty. summons.	
	Counterclaims of Third-Party Plaintiff	
Feb 29/72	Filed Answers & Counterclaims of 3rd pty defts.	
Feb 29/72	Filed First Set of Interrogs Propounded by 3rd pty defts. Allen & Co., Inc. Allen & Co., Charles Allen and Irwin H. Kramer.	
Feb 29/72	Filed First Request to produce of 3rd pty defts. Allen & Co., Inc., Allen & Co., Charles Allen and Irwin H. Kramer.	
Feb 29/72	Filed Notice of Examination by 3rd pty defts.	

Continued.

D

JUDGE MAC MAHON — JUDGE PALMIERI — 71 Civil

PROCEEDINGS	Date Order or Judgment
Mar 2-72	Filed Stip & Order extending time for production of documents to 3/29/72 So Ordered Palmieri J.
Mar 6-72	Filed Dft. Laventhol ex et al. Notice of Deposition.
Mar 8-72	Filed stip & Order extending time for dfts. & 3rd pty pltff Laventhol, Krekstein, Horwath & Horwath be adjourned to 4/19/72. So Ordered.
Mar.13-72	Filed stipulation and order adjourning deposition as indicated. So ordered. Palmieri, J.
Mar 13-72	Filed third party summons with marshal's return. Served Allen & Co. Inc. by Milton Filene-off.mgr. on 2/7/72. Allen & COo. by Milton Filene-off.mgr. on 2/7/72. Mr. Charles Allen by Milton Filene-off.mgr. on 2/7/72. Irwin H. Kramer by Milton Filene-off. mgr. 2/7/72. David Baird by Rubin Perlman-off.staff 2/2/72. ~~WERE CUMED~~ : Joe V. Meyers, VP The Firestone Group, Ltd. Richard M. Firestone, Pres/ Martin A. cott Pres.
Mar 15-72	Filed Dft. 3rd pty pltff's Interrogs. to dfts. Allen & Co., Inc., Allen & Co., Charles Allen & Irwin H. Kramer First Set.
Mar 21-72	Filed Dft. & Filed 3rd pty Pltff Laventhol, etc. Reply to the counterclaims of 3rd pty dfts. Allen & Co & Allen & Co., Inc.
Mar.24-72	Filed stipulation and order adjourning examination before trial of Gerald L. Herzfeld as indicated. So ordered. Palmieri, J.
Mar 27-72	Filed ANSWER EX BY 3rd pty dft. David Baird.
Mar 30-72	Filed Stip & Order extending time to answer complaint by 3rd pty dft. So Ordered Palmieri J. LEB
MAR 31-72	Filed answers and ojections to first set of interrogatories propounded by third party defendants Allen & Co, incorporated, Allen & Co, Charles Allen & Irwin H. Kramer.
Mar.31-72	Filed Deft-3rd pty.Pltf. Laventhol, Krekstein, Horwath & Horwath's Response to Plaintiff's Notice for Production of Documents.
Mar.31-72	Filed Deft-3rd pty.Pltf.Laventhol, Krekstein, Horwath & Horwath's Response to First Request to Produce Documents.
APR 5-72	Filed Defendant-3rd party plaintiff's interrogatories to defendants Allen & Co. Inc. etc.- Second Set
Apr 11-72	Issued add'l 3rd party summons
Apr.21-72	Filed stipulation and order adjourning examination before trial of deft-3rd pty. deft. to 5/2/72; extending defts. Allen & Co. Inc., etc. time to answer first set of interrogs. to 5/25/72, etc.etc. So ordered. Palmieri, J.
May 8-72	Filed ANSWER of Martin A. Scott to 3rd pty. complaint.
MAY 5-72	Filed additional third party summons by with marshal's return. Served Transcontinental Resources by Stephen D. Moses on 4/13/72. pro Also served Martin A. Scott by Miss Miriam Sigrip on 4/13/72. Unable to serve: Richard M. Firestone
May 16-72	Filed stip & order that examination before trial of deft-3rd pty. pltff Laventhol, Krekstein, Horwath & Horwath is adj. from 5-24 to 7-6-72 & time of defts' Allen & Co. Inc. Allen & Co., Charles Allen & Irvin Kramer to object or answer the first & second set of interrogs. of said deft is ext. to 6-15-72-So ordered-Palmieri, J
Jun 21-72	Filed stipulation and order adjourning examination before trial of deft-3rd pty-pltf. Laventhel, Krekstein, Horwath & Horwath as indicated. So ordered. Palmieri, J.
Aug 16-72	Filed stip & order that deposition of deft-3rd pty. pltff by 3rd pty.defts' Allen & Co. et al is adj. from 8-15 to 9-27-72-So ordered-Palmieri, J

JUDGE MAC MAHON

Sep 21-72 Filed pltff's notice to take deposition of deft on 9-28-72 etc.

Oct 19-72 Filed stip & order that the deposition of deft & third party pltff, Laventhol Kirkstein, Horwath, & Howath by third party deft Allen & Co, is adjourned to 11/1/72. And that the deposition of deft & third party pltff by Pltff Gerald L. Herzfeld is adjourned to 11/1/72. And that the deposition of deft & third party pltff by Gerald L. Herzfeld through other persons listed in the notice of deposition dtd 9/20/72 be adjourned sine die. So Ordered Griesa J.

Nov 1.72 Filed Stip & Order that the deposition of dft. & 3rd pty pltff. Leventhol Krekstein Horwath & Horwath by 3rd pty dfts. be adjourned to 12/12/72,etc. So Ordered Weinfeld J.

Jun 14-73 Filed third party defts,notice to take deposition of the third party pltff. on 6/27/73

7-13-73 Filed stip. & order adjourning deposition of deft. 3rd pty. pltff. to 8-30-73- MacMahon,J.

Oct. 17-73 Filed memo re: telegram to Martin A. Scott-3rd pty.deft.: "Your request for more time to appear for trial granted. You are hereby ordered to appear for trial at Noon on 10-18-73, in Room 506, U.S. Courthouse, Foley square, NY,NY, or be subject to default Judgment--MacMahon,J."

Oct. 16-73 **Trial begun & continued before Mac Mahon J. without a jury.**

Oct. 18-73 **Trial continued**

Oct. 19-73 **Trial continued**

Oct. 23-73 **Trial continued**

Oct. 25-73 **Trial continued**

Oct. 26-73 **Trial continued**

Oct. 29-73 **Trial continued and concluded (7 days), decision reserved**

Nov. 30-73 Filed post-trial brief of Laventhol,Krekstein, Horwath & Horwath

Nov. 30-73 Filed deft. & 3rd pty. pltff's proposed findings of fact

Nov. 30-73 Filed deft. & 3rd pty. pltff's proposed conclusions of law.

Dec. 5-73 Filed 3rd party pltffs' post-trial reply brief.

May 29-74 Filed OPINION #40,745--Since Allen is barred from asserting its assignors' claims, the counterclaim must be dismissed. The foregoing opinion constitutes this Court's findings of fact and conclusions of law--The Clerk of the court is directed to enter judgment--in favor of pltffs. against deft. Laventhol for damages in the amount of $97,500., with costs; in favor of 3rd pty. pltff. Laventhol against 3rd pty. deft. Allen for damages in the amount of $48,750.; in favor of 3rd pty. deft. Irving H. Kramer against 3rd pty. pltff. Laventhol dismissing the 3rd pty. complaint as against Irving H. Kramer; and in favor of 3rd pty. pltff. Laventhol against 3rd pty. deft. Allen dismissing Allen's counterclaim--So ordered--MacMahon,J.

Jun 14-74 Filed deft & 3rd pty Pltff's afft. in opposition to a motion of 3rd pty defts to amend the judgment.

Jun 14-74 Filed 3rd pty Pltff's memo. in opposition to 3rd pty defts' motion to amend certain findings and amend the judgment.

Jun.13-74 Filed Judgment & Order #74,498. Pltff (Herzfeld) have judgment against deft (Laventhal,Krekstein, Horwath & Horwath) in amount of $97,500, with costs. Third-pty pltff (Laventhol,et al) have judgment against 3rd-pty deft (Allen & Co.) for damages am't of $48,750 with costs. Third-pty deft (Kramer) have judgment against 3rd-pty pltff (Laventhal, et al) dismissing 3rd-pty complaint. Counterclaim of (Allen & Co.) against (Laventhol, et al) is dismissd Clerk.

//////////Con't on Page 6

DATE	PROCEEDINGS
Jun.5-74	Filed pltffs brief after trial.
Jun.5-74	Filed post-trial brief (reply) of Lavanthol, Krekstein & H & H.
Jun.5-74	Filed reply brief of Allen & Co. Inc.
Jun.5-74	Filed reply brief of Allen & Co., Inc.
Jun.5-74	Filed post-trial brief of Allen & Co.
Jun.5-74	Filed post-trial brief of Allen & Co.
Jun.5-74	Filed post-trial brief of Laventhol, Krekstein & H & H.
Jun.5-74	Filed trial memorandum of Lavanthol, Krekstein & H & H.
Jun.5-74	Filed supplemental memorandum of Lavanthol, Krekstein, & H & H.
Jun.5-74	Filed pltffs trial memorandum.
Jun.5-74	Filed pltffs post-trial brief of Lavanthol, Krekstein, & H & H.
Jun.5-74	Filed post-trial brief of Lavanthol, Krekstein, & H & H.
Jun.5-74	Filed by Lavanthol, Krekstein & H & H marked pleading.
Jun.5-74	Filed pltffs pre-trial order.
Jun.5-74	Filed pltffs request for findings of fact.
Jun.5-74	Filed proposed conclusions of law by Allen & Co.
Jun.5-74	Filed proposed findings of fact by Allen & Co.
Jun.5-74	Filed comments upon Lavanthol proposed findins of fact & supplemental findings of facé of Allen & Co.
Jun.5-74	Filed by Allen & Co. memorandum at trial.
JUN 24-74	Filed transcript of record of proceedings, dated 10-18-73
JUN 24-74	Filed transcript of record of proceedings, dated 10-16-73
JUN 24-74	Filed transcript of record of proceedings, dated 10-17-73
JUN 24-74	Filed transcript of record of proceedings, dated 10-23-73
JUN 24-74	Filed transcript of record of proceedings, dated 10-25-73
JUN 24-74	Filed transcript of record of proceedings, dated 10-26-73
JUN 24-74	Filed transcript of record of proceedings, dated 10-29-73
JUN 24-74	Filed transcript of record of proceedings, dated 10-15-73
Sep.13-74	Filed by Allen & Co. reply affdvt on motion to amend findings & judgment.
Sep.13-74	Filed by Allen& Co. reply memo.
Sep.13-74	Filed by deft & 3rd-pty pltff memo in opposition to 3rd-pty defts motion to amend certain findings 7 amend the judgment.
Sep.13-74	Filed pltffs notice of motion (dated 6-14-74) to amend Court's findings of fact & conclusions of law.
Sep.13-74	Filed Memo-End on motion (dated 6-14-74). See memorandum decision of this date. (9-13-74)....MAC MAHON,J.
Sep.13-74	Filed by (Allen & Co.) affdvt in support of motion (6-14-74).
Sep.13-74	Filed Memo-End. on above affdvt. See Memorandum decision of this date.....MAC MAHON,J.
Sep 13-74	Filed Memorandum Decision#41169.....Pltffs' motion to amend the Court's findings of fact and conclusions of law and the judgment of this court, ent. 6-13-74 is granted insofar as it seeks to inclrease the judgment against Leventhol, Krekstein, Horwarth & Horwath to $153,000, with interest....3rd pty deft Allen's liability in contribution to Laventhol is hereby inclreased to $75,500, plus onehalf the interest which Laventhol must pay to Pltffs:..Allen's motion to amend the judgment and the court's finding of fact is denied....Settle Judgment within 10 days aperding this court's judgment ent. 6-13-74, in accordince with this memorandum....MacMahon, J. m/p

L. HERZFELD -v- LAVENTHOL, KREKSTEIN, et al

DOCKET

CIV. 2209
MAC MAHON, J.

	FILINGS—PROCEEDINGS	AMOUNT REPORTED IN EMOLUMENT RETURNS
Oct.8-74	Filed Amended Judgment #74,800 & Order. Pltff have judgment against deft (Laventhol) in the am't of $153,000 with costs & interest at the rate of 71/2 % from 1-1-71 to 9-1-72, & 6% from 9-1-72 to date of payment. Third-pty pltff (Laventhol) have judgment against 3rd-pty deft (Allen & Co.) for damages in am't of $76,500 with costs & one-half the interest which Lavanthol must pay to pltff. Third-pty deft (Kramer) have judgment against 3rd-pty pltff (Laventhol) dismissing 3rd-pty complt. Counterclaim of (Allen & Co.) against (Laventhol) is dismissed. This Amended Judgment shall serve in place & stead of the judgment entered 6-13-74.....MAC MAHON,J. Judgment Entered, 10-9-74, Clerk m/n	
Oct 18-74	Filed 3rd pty defts and 3rd pty counterclaimants' Notice of Appeal to USCA from the amended judgment ent on 10-9-74..Notices Mailed to: Blum, Haimoff, Gerson, Lipson & Szabad----and Wilkie Farr & Gallager, on 10-21-74.	
Nov 6-74	Filed deft's & third party pltff's Notice of Appeal to USCA from the amended Judgment filed on 10-9-74... Notices mailed to: Blum Haimoff Gerson Lipson & Szabad---- and Pollack & Singer, on 11-7-74.	
Nov.6-74	Filed Supercedeas Bon in the sum of $215,000 - Fidelity & Deposit Co.	
Nov.6-74	Filed by 3rd-pty defts-3rd-pty Counterclaimants-Appellants (Allen) designation of exhibits to be included in record on appeal.	
Nov 18-74	Filed Pltff's Designation of Exhibits to be transmitted to USCA.	
Nov 19-74	Filed Deft. 3rd pty pltff's Designation of exhibits to be transmitted to USCA.	
* Dec 18-72	Filed stipulation that the deposition of defendant and third-party plaintiff, Laventhol, Krekstein, Horwath & Horwath, by third-party defendants Allen & co. etc., be adjourn from Dec. 12-72 to Dec 28-72, and said deposition to be held at the offices of Blum, Haimoff, Gersen, Lipson & Szabad, 270 Madison ave, New Yeek	
Nov. 25-74	Filed stipulation supplementing a true copy of original filed document to the U.S.C.A. (Original filed document is presently missing from file) A TRUE COPY RAYMOND F. BURGHARDT, Clerk	

D. C. 110

SUMMONS IN A CIVIL ACTION

D. C. Form No. 45 Rev. (8-69)

SUMMONS FILED MAY 18, 1971

8a

United States District Court

FOR THE

SOUTHERN DISTRICT

CIVIL ACTION FILE NO. 71-2209

JUDGE PALMIERI

GERALD L. HERZFELD,

Plaintiff

v.

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT, HOLTZMANN, WISE & SHEPARD, JAMES W. DEER, JACOBS, PERSINGER & PARKER, And LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendants

SUMMONS

To the above named Defendant :

You are hereby summoned and required to serve upon BLUM, HAIMOFF, GERSEK, LIPSON & SZABAD, plaintiff's attorney, whose address 270 Madison Avenue, New York, New York 10016 an answer to the complaint which is herewith served upon you, within 20 days after service of this summons upon you, exclusive of the day of service. If you fail to do so, judgment by default will be taken against you for the relief demanded in the complaint.

JOHN LIVINGSTON
Clerk of Court.

P. McKEEN
Deputy Clerk.

Date: May 18th, 1971

[Seal of Court]

I hereby certify and return, that on the day of 19

I received this summons and served it together with the complaint herein as follows:

MARSHAL'S FEES

Travel..... $.....

Service.....

United States Marshal.

By.....

Deputy United States Marshal.

Subscribed and sworn to before me, a this

day of , 19 .

[SEAL]

Note.—Affidavit required only if service is made by a person other than a United States Marshal or his Deputy.

No.

United States District Court
FOR THE
Southern District

GERALD L. HERZFELD,

v.

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, et al

SUMMONS IN CIVIL ACTION

Returnable not later than 20 days after service.

BLUM, HAIMOFF, GERSEN, LIPSON & SZABAD
270 Madison Avenue
New York, New York 10016
Attorney for Plaintiff.

F3Y—LK—1-16-61—20025—6863

e6

COMPLAINT FILED MAY 18, 1971

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

----------X

GERALD L. HERZFELD,

Plaintiff,

v.

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT, HOLTZMANN, WISE & SHEPARD, JAMES W. DEER, JACOBS, PERSINGER & PARKER, and LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendants.

----------X

COMPLAINT

Plaintiff, complaining of the defendants, by his attorneys, BLUM, HAIMOFF, GERSEN, LIPSON & SZABAD, alleges (on information and belief except as to Paragraphs 3, 17, 18, 19 and 20):

JURISDICTION

1. Jurisdiction of this Court over this action is based upon §22(a) of the Securities Act of 1933 (15 U.S.C. §77v[a]) and §27 of the Securities & Exchange Act of 1934 (15 U.S.C. §78aa) and upon the principle of pendent jurisdiction.

2. This action arises under §12(2) and §17(a) of the Securities Act of 1933 and §10(b) of the Securities & Exchange Act of 1934 and the Rules and Regulations of the Securities & Exchange Commission ("Commission") promulgated thereunder; and under §352-c of the General Business Law of the State of New York and under the common law. The acts of

the defendants which are hereinafter alleged took place, unless otherwise indicated, within the Southern District of the State of New York. 11a

THE PARTIES

3. GERALD L. HERZFELD is a resident of the City and County of New York and maintains an office for the transaction of business at 919 Third Avenue, New York, New York.

4. Defendant ALLEN & COMPANY, INCORPORATED ("ALLEN, INC.") was at all relevant times and still is, a corporation organized under the laws of the State of New York, with its principal place of business at 30 Broad Street, New York, New York. It is engaged primarily in the business of investment banking, underwriting and as a registered broker dealer in the sale of various types of securities to the public, both for its own account and for the accounts of others.

5. Defendant ALLEN & COMPANY ("ALLEN CO."), was at all relevant times and still is, a limited partnership organized and registered under the laws of the State of New York, with its principal place of business at 30 Broad Street, New York, New York. It is engaged primarily in the business of investment banking, underwriting and as a registered broker dealer in the sale of various types

of securities to the public both for its own account and for the accounts of others.

6. The defendant CHARLES ALLEN was at all relevant times, and still is, a General Partner of ALLEN CO., an Officer and Director of ALLEN, INC. and a major stockholder of, and controlling person in, THE FIRESTONE GROUP, LTD. ("FIRESTONE, LTD.").

7. The defendant LEE W. MEYERS was at all relevant times, and still is, a Vice President of ALLEN, INC. and at all relevant times and until December, 1970, was a Director of FIRESTONE, LTD.

8. The defendant IRWIN H. KRAMER was at all relevant times, and still is, a Vice President of ALLEN, INC.

9. FIRESTONE, LTD. was incorporated on December 26, 1968 under the laws of the State of Delaware for the purpose of conducting a business in the purchase, sale, development and management of real property and interests in real property. The principal offices of the Company are located at 342 North Rodeo Drive, Beverly Hills, California.

10. The defendant RICHARD M. FIRESTONE was at all relevant times, and still is, President and a Director of FIRESTONE, LTD.

11. The defendant MARTIN A. SCOTT was at all relevant times a Vice President and Director of

12. The defendants HOLTZMANN, WISE & SHEPARD were at all relevant times, and still are, a firm of attorneys duly admitted to practice law in the State of New York. The principal office of said law firm is located at 30 Broad Street, New York, New York.

13. The defendant JAMES W. DEER was at all relevant times, and still is, an attorney, duly admitted to practice law in the State of New York, and a member of the aforesaid law firm of HOLTZMANN, WISE & SHEPARD. The said JAMES W. DEER acted on behalf of HOLTZMANN, WISE & SHEPARD in the performance of the acts of said law firm which are hereinafter alleged.

14. The defendants JACOBS, PERSINGER & PARKER were at all relevant times, and still are, a firm of attorneys duly admitted to practice law in the State of New York. The principal office of said law firm is located at 70 Pine Street, New York, New York.

15. The defendants LAVENTHOL, KREKSTEIN, HORWATH & HORWATH were at all relevant times, and still are, a firm of certified public accountants, duly admitted to practice public accounting in the States of California and New York. Their New York office is located at 919 Third Avenue, New York, New York.

16. In or about November and December, 1969, and January, 1970, the defendants ALLEN, INC., ALLEN CO.,

CHARLES ALLEN, FIRESTONE, LTD., RICHARD M. FIRESTONE, MARTIN A. SCOTT, LEE W. MEYERS and IRWIN H. KRAMER solicited the sale of, offered for sale, and sold to the public, within the State of New York, in other states of the United States, and in Europe, securities of FIRESTONE, LTD., consisting of $7,500,000. of the 9 1/4% promissory notes of FIRESTONE, LTD. and 150,000 shares of the common stock of said Company, said securities being offered for sale and sold in Units, each Unit consisting of a note in principal amount of $250,000. and 5,000 shares of the stock at $1. per share.

17. In or about November, 1969, the defendants sold to plaintiff, through one DAVID BAIRD, acting as agent for defendants, and through IRWIN H. KRAMER, Vice President of ALLEN, INC., a portion of the securities described in Paragraph 16 hereof, consisting of $500,000. in notes and 10,000 shares of stock, in payment for which plaintiff paid a total of $510,000.; the said payment was made to defendants at 30 Broad Street, New York, New York, on or about December 16, 1969.

18. The said purchase was made in accordance with separate Note and Stock Purchase Agreements ("Agreement") dated November 10, 1969, executed by plaintiff and by DAVID BAIRD as nominee for plaintiff, which said executed Agreements were delivered to defendants at 30 Broad Street, New York, New York, on or about November 24, 1969.

19. In connection with the sale of the said

securities by defendants, as aforesaid, to the plaintiff, and pursuant to arrangement made by the said defendants, the firm of HOLTZMANN, WISE & SHEPARD acted as Special Counsel for the plaintiff GERALD L. HERZFELD and for the other purchasers of the said securities, and the firm of JACOBS, PERSINGER & PARKER acted as Counsel for FIRESTONE, LTD. 15a

20. In connection with, and in the course of, the said solicitations to purchase and offers to sell and sale, CHARLES ALLEN communicated to plaintiff, through DAVID BAIRD, acting as defendants' agent, and the said DAVID BAIRD communicated to plaintiff the following untrue statement of material fact: The said securities of FIRESTONE, LTD. were: "the hottest thing ALLEN ever had"; and the defendant IRWIN H. KRAMER communicated to plaintiff that the FIRESTONE, LTD. securities were "the best thing ALLEN ever had"; and omitted to state material facts necessary in order to make that statement, in light of the circumstances under which it was made, not misleading, and intended that plaintiff should believe and act thereon.

NON-DISCLOSURES PRIOR TO SALE

21. In connection with and in the course of the said solicitation to purchase, offer to sell and sale,

defendants omitted to state to plaintiff the following material facts, among others, known to defendants:

(a) In January, 1969 FIRESTONE, LTD. had sold 126,667 shares of stock to ALLEN, INC. and 158,000 shares to ALLEN CO. at $1. per share.

(b) In or about March, 1969, a Registration Statement and Preliminary Prospectus, dated March 12, 1969, had been filed by FIRESTONE, LTD. with the Commission covering the issuance of $16,665,000. in debentures and common stock, in which ALLEN, INC. was to act as principal underwriter, the firm of HOLTZMANN, WISE & SHEPARD were attorneys for the underwriter, and the firm of JACOBS, PERSINGER & PARKER were attorneys for FIRESTONE, LTD.; that as of November 10, 1969, the Commission had not declared said Registration Statement effective; that on November 10, 1969, an application was made by FIRESTONE, LTD. to withdraw said Registration Statement; and on November 14, 1969 said Registration Statement was withdrawn. The said Registration Statement and Preliminary Prospectus contained material factual data concerning the securities of FIRESTONE, LTD. which was not disclosed to plaintiff and the other purchasers.

(c) On October 30, 1969, FIRESTONE, LTD. had filed an S-11 Registration Statement with the Commission covering an offering of limited partnership interests (said Statement contained further factual disclosures relevant to the investment in FIRESTONE, LTD. securities, which were not disclosed to plaintiff and other purchasers.)

(d) FIRESTONE, LTD. planned to do business by purchasing real property and re-selling the same at a profit to limited partnerships in which a FIRESTONE, LTD. subsidiary would be the general partner and which would be formed for the specific purpose of purchasing each parcel of property; each such limited partnership was to be capitalized by a public sale or syndication of limited partnership interests; and that there could be no assurance that said public financing could be obtained or that such property could be publicly syndicated at a profit.

(e) In or about March, 1969, the Company had pre-filed an Offering Statement and Prospectus with the Attorney General of the State of New York covering the issuance of the securities referred to in subdivision (b) hereof; and the Attorney General had not accepted said Statement and Prospectus for filing.

(f) The method by which the Company did business consisted of the holding of seminars in major cities in the United States, open to persons interested in real estate as an investment; at the conclusion of the lectures, participants were encouraged to leave their names and addresses so that they might be offered participation in Company syndications. This method of doing business was of questionable legality, and in July, 1970, it was adjudicated that said method of doing business violated §5(a), (b)(1), and (c) of the Securities Act of 1933.

(g) On or about November 4, 1969, FIRESTONE, LTD. had advertised an offering of interests in a limited partnership in a California newspaper, which advertisement was determined to be a violation of law by the California Commissioner of Corporations, and resulted in suspension, for six days, of the security dealer license of RICHARD M. FIRESTONE.

(h) FIRESTONE, LTD. was an untried speculative enterprise whose method of doing business was of questionable legality, and defendants had no reasonable basis to believe, under the circumstances, that the Company could meet its obligations under the notes for interest and principal or that the stock had or would have, any value.

MISREPRESENTATIONS AT OR PRIOR TO CLOSING

22. Beginning on or about November 12, 1969, and from time to time thereafter, as hereinbelow alleged, the defendants communicated to plaintiff and other purchasers, expressly and by implication, the following untrue statements of material facts, and omitted to state material facts necessary in order to make the said statements, in light of the circumstances under which they were made, not misleading, and intended that plaintiff should believe and act thereon:

(a) That the securities of FIRESTONE, LTD.

were an excellent investment; the principal and interest on the notes would be paid when due; and the common stock would appreciate in value.

(b) The defendants had made a thorough and adequate investigation of, and kept under continuous review, the financial condition of FIRESTONE, LTD., and the quality and safety of the said securities.

(c) That the firm of HOLTZMANN, WISE & SHEPARD were acting as Special Counsel for plaintiff and the other purchasers; whereas, in fact, the said firm was acting as attorneys for the defendants.

(d) That the unaudited and audited financial statements submitted to plaintiff and the other purchasers reported gross sales for an eleven month period ending November 30, 1969, of $17.7 million dollars and $22.1 million dollars respectively, which included, in both cases, a fictitious sale of $15.3 million dollars; in respect of this sale, FIRESTONE, LTD., as of November 30, 1969, had made a $5,000. cash deposit and had received from an alleged "purchaser", cash of $25,000.; on the basis of these small cash deposits, both the unaudited and audited statements included and further reported "profits" of $2,030,500. as having been earned in the transaction, of which $235,000. was included as current income, and $1,795,000. was "deferred" income; the defendants had no basis to believe the sale would be closed, the sale was

never consummated, and the effect of which was that FIRESTONE, LTD. reported a fictitious sale of $15.3 million dollars and fictitious profit of $2 million dollars.

(e) That projected earnings for the 12 months ending December 31, 1969 were more than $3 million dollars, whereas, in fact, there were little or no earnings during that period.

(f) That the issuance and sale of the Units pursuant to the Agreement were exempt from the Registration and Prospectus requirements of the Securities Act of 1933, as a transaction involving a public offering; whereas, in fact, the issuance and the sale of the said Units were subject to the Registration and Prospectus requirements of the Securities Act of 1933.

(g) That the financial statement of FIRESTONE, LTD. as of November 30, 1969, had been certified by Laventhol, Krekstein, Horwath & Horwath; whereas, in fact, the financial statement was not certified by Laventhol, Krekstein, Horwath & Horwath.

(h) That FIRESTONE LTD.'s auditors had advised it that conservative accounting practices made certain adjustments necessary; whereas, in fact, both the financial statement annexed to the Agreement and the said certified financial statement, were false.

(i) On December 16, 1969, FIRESTONE, LTD. communicated to plaintiff and the other purchasers the following further false statements of material facts:

"1. Prepaid interest and prepaid management fees were adjusted upward from the amounts projected. See Note 7 to the notes to audited financial statements.

2. Sales and costs of sales increased from the amounts projected and net income was lower than projected, principally as a result of changes in closing schedules.

3. In the ordinary course of our business, certain transactions which were scheduled to close by November 30, 1969 have been carried over to December, and one transaction not originally scheduled to take place by November 30, 1969 was substantially completed by that date. See Notes 4 and 11 to the notes to audited financial statements. One transaction which is reflected in the November 30 audited financial statements has been treated as producing deferred gross profit rather than current gross profit. While the comination of current and deferred income is actually higher than projected ($1,411,557 as compared with $1,360,000 projected), the shift of $1,795,500 of gross profit on this transaction from a current basis to a deferred basis by the auditors has reduced current net income below that originally projected. Had the audited statements been prepared subsequent to January 30, 1970, when the final payment on this transaction is due, the current income for the period would have been greater than that projected.

4. Net income for the period ended November 30, 1969 is shown on the audited statement as $66,916 as against $315,000 projected. The transactions originally scheduled to close in November will now close in December which will make up the difference in current net income between that projected and the actual. Deferred income shown on the audited balance sheet has been increased to $2,834,133 as against $1,421,000 projected. A breakdown of the components of the deferred

income account is shown in the audited financial statements. The differential between the net worth shown on the projected balance sheet and the net worth shown on the audited balance sheet is almost entirely attributable to the reclassification of income from a current basis to a deferred basis.

5. The rescheduling by the Company of its closings as aforesaid has resulted in a decrease in the assets of the Company with a corresponding decrease in liabilities from those projected.

We believe that none of these changes have resulted or will result in an adverse change in our financial condition or the results of our operations."

In the said communication, plaintiff and the other purchasers were further offered an opportunity to rescind their purchases on or before January 9, 1970.

Neither the plaintiff nor any of the other purchasers were able to exercise an informed judgment as to the offer of rescission since said representations created the false impression that FIRESTONE, LTD. had earned approximately $3 million dollars in 1969; that any changes between the unaudited statements and the certified statements were of a technical nature; that the differences between current income and deferred income were concerned with accounting theory and not with fact; and that the current and deferred income reported reflected actual operating profits; whereas, in fact, FIRESTONE, LTD. had earned little or no profit in 1969.

(j) The financial statement submitted by the

accounting firm of Laventhol, Krekstein, Horwath & Horwath was false in the following respects:

(i) The certificate signed by the accounting firm stated that the financial statements fairly stated the financial position of FIRESTONE, LTD. and its subsidiaries in conformity with accepted accounting principles "subject to the collectibility of the balance receivable on the contract of sale (see Note 4 of Note 2 of the financial statement)". The said "balance receivable" was $4,965,250.; neither the defendants nor the accountants had any basis to believe that the said payment would be made when due; and, in fact, the said payment was not made when due.

(ii) The said statement set forth a schedule of deferred income in the aggregate sum of $2,834,133., representing, thereby, that FIRESTONE, LTD. had earned this substantial profit in less than one year of operations and that the income was being deferred for accounting reasons; whereas, the said income had not been earned and defendants had no reason to believe that said income would be realized by the Company.

(iii) The said statement reflected transactions as involving the purchase and sale of real property and interests in real property and set forth profits in said transactions; whereas the said purchases and sales were "paper" transactions, involving small cash

deposits by purchasers and seller, and in respect of which, defendants had no reason to believe that the transactions would, in fact, be consummated or that the profits would, in fact, be realized.

(k) On or about December 16, 1969, the defendants, through their attorneys, JACOBS, PERSINGER & PARKER, certified to the plaintiff and to the other purchasers that:

> "(iv) based upon the representations of the Company set forth in Paragraph 5(i) of the Agreements and the representations of each Purchaser set forth in Paragraph 6 of the Agreements, the issuance, sale and delivery to the Purchasers of the Units do not, under existing law, require the registration of the Units or any part thereof, under the Securities Act of 1933, as amended;...
>
> (vi) no authorization, approval, consent or license of any regulatory body or authority is required for the valid authorization, issuance, sale and delivery of the Units, or any part thereof;...
>
> (x) we have no knowledge of any action or proceeding pending or threatened against the Company or any Subsidiary before any court or administrative agency which could result in any material adverse change in the business or condition of the Company; and..."

The said statements were untrue to the knowledge of the defendants in that clearance with the Commission and with the Attorney General of the State of New York was necessary for the valid sale and delivery of the securities; and in that defendants had knowledge of proceedings pending before the Commission in which it could be determined that the method of business being conducted by the Company was illegal and which could thereby result in a material adverse change in the business and condition of the Company.

BREACH OF WARRANTIES
AND REPRESENTATIONS
IN AGREEMENT

23. The defendants violated the following conditions, covenants, representations and warranties contained in the Agreement dated November 10, 1969.

(a) It was represented and warranted that:

> "(i) Within the past three years, neither the Company nor any agent acting on its behalf has offered the Notes or the Stock or any substantially similar security or any part thereof from, any person in a manner or under circumstances which would subject the issuance or sale of the Units to the provisions of Section 5 of the Securities Act, and neither the Company nor any agent acting on its behalf has taken or will take any other action which would subject the issuance or sale of the Units to the provisions of said Section 5."

The defendants violated said representation and warranty in that:

(i) the offering of the notes and stock was made under circumstances which subjected the issuance and sale of said securities to the provisions of Section 5 of the Securities Act of 1933; and

(ii) in or about March, 1969, as hereinabove alleged, the defendants undertook to offer substantially similar securities to the public by the filing of a Registration Statement and Preliminary Prospectus with the Commission, and with the Attorney General of the State of New York, and copies of which said Preliminary

Prospectus were distributed to brokers and others for the purpose of interesting the financial community in the purchase of said securities.

(b) It was represented and warranted that:

> "(j) The Company intends to use the net proceeds from the sale of the Units as follows: approximately $1,600,000. to pay income taxes of the Company due April, 1970, in respect of deferred income."

The said representation was designed fraudulently to induce the plaintiff and other purchasers to believe that FIRESTONE, LTD. was then a successful and highly profitable business, having earned more than $3,500,000. in eleven months, whereas FIRESTONE, LTD. had little or no taxable income; defendants knew that the Company would not require $1,600,000. to pay income taxes in April, 1970; and in fact, the funds were not used for that purpose.

(c) Defendants represented and warranted that Exhibit B annexed to the Agreement, being the Consolidated Projected Balance Sheet and Statement of Income for the eleven months ended November 30, 1969,

> "...will be correct and complete and will fairly present the financial condition of the Company and its Subsidiaries as at November 30, 1969 and the results of their operations for the eleven months then ended, subject to audit and year-end adjustments.";

that any liabilities not reflected on the balance sheet would not "have any material adverse effect upon the Company"; and that the said "financial statements have been

prepared in accordance with generally accepted accounting practice"; whereas the said financial statements were false and fraudulent, as the defendants knew or should have known, in the following respects:

(i) The Balance Sheet stated that "deferred income consists of $788,000 in prepaid management fees and $1,914,000 in prepaid interest", aggregating $2,702,000; whereas, as defendants knew, FIRESTONE, LTD. had little or no income.

(ii) The Projected Statement of Income stated that the Company had "projected deferred income of $2,702,000"; that taxes on deferred income (current portion) was "$1,080,000 (current portion)"; and that taxes on "deferred income was $577,000"; the said statements were falsified to create the impression that the Company's operations in 1969 were substantially profitable; whereas the Company was operating at little or no profit.

(iii) The Projected Statement of Income stated that the Company had combined net income, after income taxes, of $1,360,000; whereas the Company had little or no income.

(f) In the said Agreement, the defendants warranted and represented that:

> "(d) There are no actions or proceedings pending or, to the knowledge of the Company, threatened against the Company or its Subsidiaries before any court or administrative agency which might, alone or

> in the aggregate, result in any material adverse change in the business or condition of the Company. To the best of its knowledge, the Company and its Subsidiaries are in compliance with all applicable laws to which they are subject."

In fact, there were then pending, or threatened, to the knowledge of defendants, proceedings before the Commission, in which it was determined that the Company's method of doing business was unlawful, thereby resulting in a material adverse change in the business and condition of the Company.

24. A further artifice and scheme to defraud by defendants was the inclusion in the Agreement of a provision that if the Company, prior to June 30, 1971, shall split its common stock in the ratio of 2 for 1, and make a public offering of securities at a price, after giving effect to the stock split, of not less than $25. per share, the plaintiff and the other stockholders were required to include in the public offering, up to 1/2 the number of shares owned by any stockholder.

This provision served no corporate purpose; was included solely as a "come-on"; and was designed to induce the plaintiff and other purchasers to believe that the common stock of the Company, for which the plaintiff and other purchasers had paid $1. per share, would be offered to the public at $50. per share; which representation, under the circumstances, was false and fraudulent in that

defendants had no reasonable basis to believe, and did not, in fact, believe, that in a period of 19 months, the stock of the Company could be sold to the public at $50. per share.

MISREPRESENTATIONS
SUBSEQUENT TO CLOSING

25. On or about February 27, 1970, the defendant, FIRESTONE, LTD. delivered to the plaintiff and to the other purchasers a consolidated balance sheet and statement of income and retained earnings purporting to cover the period from December 26, 1968 to December 31, 1969, which was false and fraudulent in that it set forth additional sales and profits, stated that the Company had deferred income of $3,016,031. and that it had earned gross sales profit of $2,660,556. and management fees and interest income of $568,183.; which said statements were designed to induce the plaintiff and the other purchasers to believe that the Company was earning substantial profits; whereas, in fact, many of the alleged sales were merely "paper" transactions, which defendants had no reason to believe would be consummated and which, in fact, were not consummated.

26. On May 28, 1970, the defendants delivered to the plaintiff and other purchasers an Annual Report to Shareholders for the year 1969, which was false and fraudulent in the following respects:

(a) In the President's Letter, it was stated that FIRESTONE, LTD. had had difficulties dealing with

certain tax law changes; whereas, in fact, the difficulties which the Company had were concerned with its method of conducting business, which ultimatley was determined by the Commission to be in violation of the Securities Act of 1933.

(b) The said Statement was further false in that it reported as "deferred gross profit" the sum of $1,795,000. as having been earned in the transaction described in Paragraph 18(d) hereof, though no profit had in fact been realized and it was further stated that the date for payment by the purchaser, of $4,965,250. had been extended to July 1, 1970, which statement was made to induce the plaintiff and other purchasers to believe that this profit would be realized on the extended date; whereas, defendants knew, or should have known, that the contract would not be closed and that the profit would not be realized.

(c) The President's Letter was further false and fraudulent in that it failed to disclose that the Commission had under investigation the procedures followed by the Company in the holding of seminars as a device for effecting public distribution of participations in its projected limited partnership syndications; and in that it set forth an imaginary network of sales outlets which were to be created and which would enable the Company to sell its syndicated participations through a non-exist-

ent network of real estate brokers and stock brokers.

(d) The consolidated statement of income was false and fraudulent in that it set forth gross profit on sales of $2,636,107. which had not been, and never were, realized; and management and interest income of $1,888,613. which had not been and never was received by the Company.

27. For the purpose of further deceiving the plaintiff and other purchasers, the defendants delivered with the Annual Report above described, a separate statement which was described as follows:

> "This Statement has been separated to eliminate any possible confusion with the one audited by the Certified Public Accountant which does not include deferred income."

This statement was false in that the statement audited by the Certified Public Accountant did include deferred income but described it as such, whereas this accompanying statement, purportedly included to avoid confusion, falsely stated that the Company had earned $1,631,234. in the nine months ended January 3, 1970, which the Company had not earned.

28. In or about the Spring of 1970, the plaintiff met with the defendants LEE W. MEYERS and IRWIN H. KRAMER at the offices of ALLEN, INC.; plaintiff inquired of the defendant LEE W. MEYERS concerning the business of FIRESTONE, LTD.; and defendant LEE W. MEYERS stated to plaintiff that the business of FIRESTONE, LTD. was "just great", whereas, in fact, as defendant LEE W. MEYERS well knew, on

should have known, FIRESTONE, LTD. was operating at a loss; its method of doing business was under challenge by the Commission; and the stock had little or no value.

$2 MILLION DOLLAR "BAIL-OUT"
OF ALLEN CO. BY FIRESTONE, LTD.

29. In or about 1970, defendants conspired to effect a "bail-out" of ALLEN CO. in respect of an investment previously made by ALLEN CO. in real estate which had proved unprofitable; as part of said scheme and in furtherance thereof, FIRESTONE, LTD."purchased" the said real property from ALLEN CO. for $2,000,000., though said property had little or no value.

30. At alltimes relevant hereto, defendants had notice of, knew, had means of knowing, and could and should have known all material facts and circumstances concerning the management, operations, financial dealings and financial conditions of FIRESTONE, LTD.

31. The plaintiff did not know that the said statements and representations of defendants to plaintiff were materially untrue or incomplete as aforesaid; and at all times relevant hereto, defendants ALLEN, INC., ALLEN CO., and CHARLES ALLEN, IRWIN H. KRAMER and LEE W. MEYERS held themselves out to the public and to plaintiff as expert, skilled and careful in the sale and recommending for sale, of securities and said defendants sought to have the public and the plaintiff rely on their claimed expertise,

skill and care, and plaintiff, in the exercise of due care relied upon the claimed expertise, skill and care of defendants and upon the said statements and representation of defendants and plaintiff was thereby induced to purchase the said securities.

32. On or about March 1, 1971, FIRESTONE, LTD. defaulted in the payment of interest then due, and on or about March 30, 1971, an involuntary petition in bankruptcy was filed against FIRESTONE, LTD. in the Federal Bankruptcy Court in the Central District U.S. Courthouse, Los Angeles, California; by reason whereof, the securities sold to plaintiff are in default and are of no value.

33. All of the foregoing allegations are hereby incorporated by reference in each of the claims asserted herein as if fully set forth therein.

AS AND FOR A
FIRST CLAIM

34. This claim is instituted pursuant to §12(1) of the Securities Act of 1933 (15 U.S.C. §77L) for rescission of the said sales of securities to plaintiff by defendants or for damages, together with the costs of suit and reasonable attorneys' fees, as a result of defendants' violation of §12(1) of the said Act as herein alleged.

35. No Registration Statement was in effect for the said securities at the time of their said sales or

offer of sale by defendants to plaintiff.

36. The said sales and offers of sale to plaintiff by defendants violated §12(1) of the Securities Act of 1933 in that they constituted or involved offers or sales of securities in violation of §5 of the Securities Act of 1933.

37. The said offers or sales violated §5 of the Securities Act of 1933 in that they were made by defendants who made use of means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to sell said securities through the use or medium of a prospectus or otherwise or who carried or caused to be carried through the mails or in interstate commerce by means or instruments of transportation, the said securities for the purpose of sale or for delivery after sale.

38. By reason of the fraudulent acts of defendants as set forth in Paragraphs 20, 21, 22 and 23 hereof, defendants are estopped to plead the statute of limitation imposed by §13 of the Securities Act of 1933; and plaintiff has commenced this action within one year after plaintiff discovered the facts constituting the violations sued upon.

39. Plaintiff hereby tenders the said securities to defendants.

40. By reason of the foregoing, plaintiff has been damaged in the amount of $510,000.

AS AND FOR A
SECOND CLAIM

41. This claim is instituted pursuant to §12(2) of the Securities Act of 1933 (15 U.S.C. §77L) for rescission of the said sales of securities to plaintiff by defendants or for damages, together with the costs of suit and reasonable attorneys' fees, as a result of defendants' violations of §12(2) of the said Act as herein alleged.

42. The said sales to plaintiff by defendants violated §12(2) of the Securities Act of 1933 in that they constituted or involved offers or sales of securities by the use of means or instruments of transportation or communication in interstate commerce or of the mails, by means of prospectuses or oral communications, which included, unknown to plaintiff, untrue statements of material facts or omissions to state material facts necessary, in order to make the statements, in light of the circumstances under which they were made, not misleading.

43. Plaintiff has commenced this action within one year of the discovery of the said untrue statements and omissions.

44. Plaintiff hereby tenders the said securities to defendants.

45. By reason of the foregoing, plaintiff has been damaged in the amount of $510,000.

AS AND FOR A
THIRD CLAIM

46. This claim is instituted pursuant to §17(a) of the Securities Act of 1933 (15 U.S.C. §77q) for rescission of the said sales of securities or for damages, together with the costs of suit and reasonable attorneys' fees as a result of defendants' violations of §17(a) of said Act as herein alleged.

47. Defendants, in contravention of §17(a) of the Securities Act of 1933, offered and sold to plaintiff securities by the use of means or instruments of transportation or communication in interstate commerce or by use of the mails, and directly or indirectly (a) employed a device, scheme or artifice to defraud plaintiff; (b) obtained money or property from plaintiff by means of untrue statements of material facts or omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in transactions, practices, and a course of business which operated as a fraud and deceit on plaintiff.

48. Plaintiff hereby tenders the said securities to defendants.

49. By reason of the foregoing, plaintiff has been damaged in the amount of $510,000.

AS AND FOR A
FOURTH CLAIM

50. This claim is instituted pursuant to §10(b) of the Securities Exchange Act of 1934 (15 U.S.C. §78j) and Rule 10b-5 (17 C.F.R. §240.10b-5) promulgated thereunder for rescission of the said sales of securities or for damages, together with the costs of suit and reasonable attorneys' fees, as a result of defendants' violations of the foregoing Act and Rule.

51. Defendants, in contravention of §10b of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder by use of means or instrumentalities of interstate commerce or the mails (a) employed a device, scheme or artifice to defraud plaintiff; (b) made untrue statements of material facts or omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in transactions, practices and a course of business which operated as a fraud and deceit on plaintiff.

52. Plaintiff hereby tenders the said securities to defendants.

53. By reason of the foregoing, plaintiff has been damaged in the amount of $510,000.

AS AND FOR A
FIFTH CLAIM

54. This action is instituted pursuant to §352-c of the General Business Law of the State of New York.

55. Defendants in contravention of §352-c of the General Business Law of the State of New York, used the following acts or practices to induce or promote the issuance, distribution, exchange, purchase, negotiation, and sale of the said securities of FIRESTONE, LTD. to plaintiff within and from New York State: (a) fraud, deception, concealment, suppression and false pretense; (b) promises and representations as to the future which were beyond reasonable expectation and unwarranted by existing circumstances; (c) representations or statements which were false, where defendants (i) knew the truth; or (ii) with reasonable effort could have known the truth; Or (iii) made no reasonable effort to ascertain the truth; or (iv) did not have knowledge concerning the representations or statements made.

56. By reason of the foregoing, plaintiff has been damaged in the amount of $510,000.

AS AND FOR A
SIXTH CLAIM

57. The said untruths and omissions were intentionally, knowingly, recklessly and fraudulently made by defendants to plaintiff and the public at large to induce plaintiff and the public to rely upon defendants' statements as true and complete in all respects and in reliance thereon to purchase the said securities to their detriment and to the financial benefit of defendants, and the plaintiff relied on the said untruths and omissions and plaintiff was thereby induced to purchase the said securities.

58. By reason of the foregoing, plaintiff has been damaged in the amount of $510,000.

59. By reason of the wilfull and reckless misconduct of the defendants as aforesaid, plaintiff seeks, in addition, punitive damages in the sum of $1,000,000.

AS AND FOR A
SEVENTH CLAIM

60. Defendants had a duty to plaintiff to ascertain the actual financial condition of FIRESTONE, LTD. at the time it offered its said securities for sale and to inform plaintiff of the said actual financial condition.

61. Defendants negligently and carelessly failed and refused to perform its duty of ascertaining the actual financial condition of FIRESTONE, LTD. at the time it offered the said securities for sale and informing the plain-

tiff of the said actual financial condition.

62. By reason of the foregoing and without any negligence of the plaintiff contributing thereto, plaintiff has been damaged in the amount of $510,000.

WHEREFORE, plaintiff demands:

1. Judgment in its favor:

(a) Rescinding the defendants' sale of said FIRESTONE, LTD. securities to plaintiff; and

(b) Compelling defendants to repay to plaintiff all consideration received by defendants from plaintiff for said securities, together with interest thereon; or

(c) Alternatively, awarding damages to plaintiff in the amount of $510,000., together with interest thereon; and

(d) Compelling defendants to pay to plaintiff the sum of $1,000,000. as punitive damages.

2. The costs, disbursements and expenses of this action, including reasonable attorneys' fees;

3. Such other and further relief as may be necessary and appropriate.

Paul S. Lipson, Of Counsel

BLUM, HALMOFF, GERSEN, LIPSON & SZABAD
Attorneys for Plaintiff
Office and Post Office Address:
270 Madison Avenue
New York, New York 10016
Tel. No. (212) 685-6333

NOTICE OF ENTRY

.EASE TAKE NOTICE that the
a true-certified-copy of a

ered in the office of the clerk of

19

19

Yours, etc.

HAIMOFF, GERSEN, LIPSON & SZABAD

for

ffice and Post Office Address
270 Madison Avenue
New York, N. Y. 10016

for

NOTICE OF SETTLEMENT

LEASE TAKE NOTICE that

the within is a true copy will be
for settlement to Mr. Justice

Justices of the within named Court

day of 19
M.

19

Yours, etc.

HAIMOFF, GERSEN, LIPSON & SZABAD

for

ffice and Post Office Address
270 Madison Avenue
New York, N. Y. 10016

for

Index No..... 19

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. HERZFELD,

Plaintiff,

v.

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT, HOLTZMANN, WISE & SHEPARD, JAMES W. DEER, JACOBS, PERSINGER & PARKER and LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendants.

COMPLAINT

BLUM, HAIMOFF, GERSEN, LIPSON & SZABAD
Attorneys for PLAINTIFF
Office and Post Office Address
270 Madison Avenue
New York, N. Y. 10016
MU 3-6383

To Esq.,

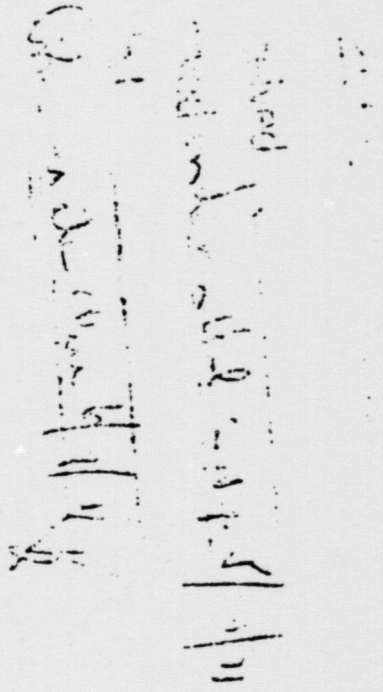
Attorney for

Service of a copy of the within

is hereby admitted.

Dated, N. Y., 19

Attorney for



ANSWER OF DEFENDANT LAVENTHOL, KREKSTEIN, HORWATH AND HORWATH FILED JULY 23, 1971

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. HERZFELD, Plaintiff, -against- THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT, HOLTZMANN, WISE & SHEPARD, JAMES W. DEER, JACOBS, PERSINGER & PARKER, and LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, Defendants.	71 Civ. 2209 (ELP) ANSWER

Defendant LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ("LKH&H"), by its attorneys, WILLKIE FARR & GALLAGHER, for its answer to the Complaint, alleges the following:

1. Denies each and every allegation contained in paragraph 1 of the Complaint except admits that plaintiff contends that jurisdiction of the Court is based on Section 22(a) of the Securities Act of 1933 (15 U.S.C. Section 77v[a]), Section 27 of the Securities Exchange Act of 1934 (15 U.S.C. Section 78aa) and upon the principles of pendent jurisdiction.

2. Denies each and every allegation contained in paragraph 2 of the Complaint except admits that plaintiff purports to assert claims under Sections 12(2) and 17(a) of the Securities Act of 1933, Section 10(b) of the Securities

Exchange Act of 1934 and the Rules and Regulations of the Securities and Exchange Commission promulgated thereunder and under Section 352-c of the General Business Law of the State of New York and under the common law.

3. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 3 of the Complaint.

4. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 4 of the Complaint.

5. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 5 of the Complaint.

6. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 6 of the Complaint.

7. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 7 of the Complaint.

8. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 8 of the Complaint.

9. Denies knowledge or information sufficient to

form a belief as to the truth of each and every allegation contained in paragraph 9 of the Complaint.

10. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 10 of the Complaint.

11. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 11 of the Complaint.

12. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 12 of the Complaint.

13. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 13 of the Complaint.

14. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 14 of the Complaint.

15. Admits the allegations contained in paragraph 15 of the Complaint.

16. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 16 of the Complaint.

17. Denies each and every allegation contained in

paragraph 17 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 17 of the Complaint insofar as it relates to other defendants.

18. Denies each and every allegation contained in paragraph 18 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 18 of the Complaint insofar as it relates to other defendants.

19. Denies each and every allegation contained in paragraph 19 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 19 of the Complaint insofar as it relates to other defendants.

20. Denies each and every allegation contained in paragraph 20 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 20 of the Complaint insofar as it relates to other defendants.

21. Denies each and every allegation contained in

paragraph 21 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 21 of the Complaint insofar as it relates to other defendants.

22. Denies each and every allegation contained in paragraph 22 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 22 of the Complaint insofar as it relates to other defendants.

23. Denies each and every allegation contained in paragraph 23 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 23 of the Complaint insofar as it relates to other defendants.

24. Denies each and every allegation contained in paragraph 24 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 24 of the Complaint insofar as it relates to other defendants.

25. Denies each and every allegation contained in

paragraph 25 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 25 of the Complaint insofar as it relates to other defendants.

26. Denies each and every allegation contained in paragraph 26 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 26 of the Complaint insofar as it relates to other defendants.

27. Denies each and every allegation contained in paragraph 27 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 27 of the Complaint insofar as it relates to other defendants.

28. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 28 of the Complaint.

29. Denies each and every allegation contained in paragraph 29 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 29 of the Complaint insofar as it relates to other defendants.

30. Denies each and every allegation contained in paragraph 30 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 30 of the Complaint insofar as it relates to other defendants.

31. Denies each and every allegation contained in paragraph 31 of the Complaint insofar as it relates to defendant LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 31 of the Complaint insofar as it relates to other defendants.

32. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 32 of the Complaint.

33. In response to paragraph 33 of the Complaint, defendant LKH&H repeats and realleges each and every allegation contained in paragraphs 1 through 32 herein with the same force and effect as if herein fully set forth and incorporates them all in answer to each of the claims asserted by the plaintiff.

34. Denies each and every allegation contained in paragraph 34 of the Complaint insofar as it relates to LKH&H but denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained

in paragraph 34 of the Complaint insofar as it relates to other defendants and admits that plaintiff purports to assert claims under Section 12(1) of the Securities Act of 1933 (15 U.S.C. Section 77L).

35. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 35 of the Complaint except denies that defendant LKH&H sold or offered to sell any securities whatsoever to the plaintiff.

36. Denies each and every allegation contained in paragraph 36 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 36 of the Complaint insofar as it relates to other defendants.

37. Denies each and every allegation contained in paragraph 37 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 37 of the Complaint insofar as it relates to other defendants.

38. Denies each and every allegation contained in paragraph 38 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 38 of the Complaint insofar as it relates to other defendants.

39. Admits that plaintiff alleges that he tenders the securities to defendants.

40. Denies each and every allegation contained in paragraph 40 of the Complaint.

41. Denies each and every allegation contained in paragraph 41 of the Complaint insofar as it relates to LKH&H but denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 41 of the Complaint insofar as it relates to other defendants and admits that plaintiff purports to assert claims under Section 12(2) of the Securities Act of 1933 (15 U.S.C. Section 77L).

42. Denies each and every allegation contained in paragraph 42 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 42 of the Complaint insofar as it relates to other defendants.

43. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 43 of the Complaint.

44. Admits that plaintiff alleges that he tenders the securities to defendants.

45. Denies each and every allegation contained in paragraph 45 of the Complaint.

46. Denies each and every allegation contained in paragraph 46 of the Complaint insofar as it relates to LKH&H but denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 46 of the Complaint insofar as it relates to other defendants and admits that plaintiff purports to assert claims under Section 17(a) of the Securities Act of 1933 (15 U.S.C. Section 77q).

47. Denies each and every allegation contained in paragraph 47 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 47 of the Complaint insofar as it relates to other defendants.

48. Admits that plaintiff alleges that he tenders the securities to defendants.

49. Denies each and every allegation contained in paragraph 49 of the Complaint.

50. Denies each and every allegation contained in paragraph 50 of the Complaint insofar as it relates to LKH&H but denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 50 of the Complaint insofar as it relates to other defendants and admits that plaintiff

purports to assert claims under Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. Section 78j) and Rule 10b-5 (17 C.F.R. Section 240.10b-5) promulgated thereunder.

51. Denies each and every allegation contained in paragraph 51 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 51 of the Complaint insofar as it relates to other defendants.

52. Admits that plaintiff alleges that he tenders the securities to defendants.

53. Denies each and every allegation contained in paragraph 53 of the Complaint.

54. Denies each and every allegation contained in paragraph 54 of the Complaint insofar as it relates to LKH&H but denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 54 of the Complaint insofar as it relates to other defendants and admits that plaintiff purports to assert claims under Section 352-c of the General Business Law of the State of New York.

55. Denies each and every allegation contained in paragraph 55 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation

contained in paragraph 55 of the Complaint insofar as it relates to other defendants.

56. Denies each and every allegation contained in paragraph 56 of the Complaint.

57. Denies each and every allegation contained in paragraph 57 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 57 of the Complaint insofar as it relates to other defendants.

58. Denies each and every allegation contained in paragraph 58 of the Complaint.

59. Denies each and every allegation contained in paragraph 59 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 59 of the Complaint insofar as it relates to other defendants except admits that plaintiff purports to seek punitive damages in the sum of $1,000,000.

60. Denies each and every allegation contained in paragraph 60 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 60 of the Complaint insofar as it relates to other defendants.

61. Denies each and every allegation contained in paragraph 61 of the Complaint insofar as it relates to LKH&H and denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 61 of the Complaint insofar as it relates to other defendants.

62. Denies each and every allegation contained in paragraph 62 of the Complaint.

WHEREFORE, defendant LAVENTHOL KREKSTEIN HORWATH & HORWATH demands judgment dismissing the Complaint as against it together with the costs and disbursements of this action.

WILLKIE FARR & GALLAGHER
Attorneys for Defendant
Laventhol Krekstein Horwath & Horwath

By Louis G. Gross
(A Member of the Firm)

Office & P. O. Address
One Chase Manhattan Plaza
New York, New York 10005

OFFICIAL RECORD

ANSWER OF DEFENDANTS ALLEN & CO., INC.; ALLEN & CO.; CHARLES ALLEN: LEE W. MEYER & IRWIN H. KRAMER, FILED JULY 30, 1971

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., et al.,

Defendants.

71 Civ. 2209 (ELP)

Answer of Defendants
Allen & Company, Incorporated,
Allen & Company, Charles Allen,
Lee W. Meyers and Irwin H. Kramer

1. Defendants Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyers and Irwin H. Kramer deny each and every allegation of the Complaint except as expressly admitted or otherwise specifically denied as follows:

Paragraph of Complaint	Specific Respon.
3, 39	Deny knowleage of information sufficient to form a belief as to the truth thereof.
4	Admit that Allen & Company, Incorporated ("Allen Inc.") was and is a corporation organized under the laws of the State of New York, with

Paragraph of Complaint	Specific Response
4 (continued)	its principal place of business at 30 Broad Street, New York, New York, and that it was and is engaged in the business of investment banking, underwriting and as a registered broker-dealer in the sale of various types of securities.
5	Admit that Allen & Company ("Allen Co.") was and is a limited partnership organized and registered under the laws of the State of New York, with its principal place of business at 30 Broad Street, New York, New York; and that it is engaged in the business of investment banking, underwriting and as a registered broker-dealer in the sale of various types of securities.
6	Admit that Charles Allen ("Mr. Allen") was and is a General Partner of Allen Co. and a director of Allen Inc.

Paragraph of Complaint	Specific Response
7, 8, 10, 11	Admit.
9, 14, 15, 35	Admit on information and belief.
13	Admit on information and belief that James W. Deer was and is an attorney duly admitted to the practice of law in the State of New York, and a member of the law firm of Holtzmann, Wise & Shepard and that insofar as he did any of the acts alleged in the Complaint he did them on behalf of said law firm.
17	Admit on information and belief that about November 1969, The Firestone Group, Ltd. ("Firestone") sold to plaintiff securities of Firestone consisting of notes and shares of stock; and that payment therefor was made at 30 Broad Street, New York, New York.

Paragraph of Complaint	Specific Response
18	Admit on information and belief that the said purchase of securities was made pursuant to a certain Note and Stock Purchase Agreement dated November 10, 1969, which was executed by plaintiff and delivered on or about December 16, 1969.
19	Admit on information and belief that Holtzmann, Wise & Shepard acted as special counsel for plaintiff and others in connection with the sale to them of securities of Firestone and that the firm of Jacobs, Persinger and Parker acted as counsel for Firestone.
28	Admit that in or about the spring of 1970, plaintiff met with Lee W. Meyers and Irwin H. Kramer at the offices of Allen Inc.

Paragraph of Complaint	Specific Response
32	Admit on information and belief that on or about March 1, 1971, Firestone defaulted in the payment of interest then due, and that on or about March 30, 1971, an involuntary petition in bankruptcy was filed against Firestone in Federal Bankruptcy Court in the Central District United States Courthouse, Los Angeles, California, and that by reason thereof the securities of Firestone sold to plaintiff are in default.

First Affirmative Defense

2. The Complaint fails to state a claim upon which relief can be granted.

Second Affirmative Defense

3. This action is barred by the applicable statutes of limitation and by plaintiff's laches.

Third Affirmative Defense

4. Plaintiff is estopped and otherwise barred from maintaining this action in that, at all times relevant hereto, he had full knowledge of all material facts relating to the sale of Firestone securities to him.

Fourth Affirmative Defense

5. Plaintiff is estopped and otherwise barred from maintaining this action, in that he purchased the said securities under false pretenses and by means of false representations.

Wherefore, defendants Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyers and Irwin H. Kramer demand judgment in their favor dismissing the Complaint, together with the costs and disbursements of this action and for their reasonable counsel fees.

Yours, etc.

Pollack & Singer

By: _____
(a member of the firm)
Attorneys for Defendants
Allen & Company, Incorporated
Allen & Company, Charles Allen,
Lee W. Meyers and Irwin H. Kramer
Office & P.O. Address
111 Broadway
New York, New York 10006
(212) WO 4-5770

71 Civ. 2209 (ELP)

United States District Court: Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., et al.,

Defendants.

Answer of Defendants Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyers and Irwin H. Kramer

POLLACK & SINGER
111 BROADWAY
NEW YORK, N. Y. 10006
WORTH 4-5770

ATTORNEYS FOR Defendants Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyers, and Irwin H. Kramer

OFFICE RECORD

Received 7/29/71

Served

Filed

Answer on Behalf of Defendants 9/15/71 PJ Inc

STIPULATION AND ORDER DISMISSING ACTION ON MERITS WITH PREJUDICE AND COSTS AGAINST ALL DEFENDANTS EXCEPT LAVENTHOL, KREKSTEIN, HORWATH & HORWATH --MEMORANDUM ENDORSED ON STIPULATION SETTING STIPULATION ASIDE FILED NOVEMBER 24, 1971 62a

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

71 Civ. 2209 (ELP)

The Firestone Group, Ltd., Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyers, Irwin H. Kramer, Richard M. Firestone, Martin A. Scott, Holtzmann, Wise & Shepard, James W. Deer, Jacobs, Persinger & Parker, and Laventhol, Krekstein, Horwath & Horwath,

Defendants.

Stipulation

1. It is stipulated and agreed by and between the plaintiff and all defendants herein except Laventhol, Krekstein, Horwath & Horwath, that this action be and hereby is dismissed on the merits, with prejudice and without costs, as against all defendants except Laventhol, Krekstein, Horwath & Horwath.

2. It is further stipulated and agreed by and between the plaintiff and all defendants herein except Laventhol, Krekstein, Horwath & Horwath that the plaintiff will not seek pre-trial discovery of any kind against any of the said defendants and will not call any of said defendants as witnesses at the trial, if any, of this action.

3. It is further stipulated and agreed by and between the plaintiff and all defendants herein except Laventhol, Krekstein, Horwath & Horwath, that the caption of this action shall be amended to delete the names of all defendants except Laventhol, Krekstein, Horwath & Horwath.

Dated: New York, New York
November 3, 1971

Blum, Haimoff, Gersen, Lipson & Szabad

By: _____
(a member of the firm)
Attorneys for Plaintiff

Pollack & Singer

By: _____
(a member of the firm)
Attorneys for Defendants
Allen & Company, Incorporated,
Allen & Company, Charles Allen,
Lee W. Meyer, and Irwin H. Kramer

Holtzmann, Wise & Shepard

By: _____
(a member of the firm)
Attorneys for Defendants
Holtzmann, Wise & Shepard
James W. Deer and
The Firestone Group, Ltd.

D'Amato, Costello & Shea

By: _____
(a member of the firm)
Attorneys for Defendant
Jacobs, Persinger & Parker

Lipper, Keeley, Katcher,
Lowey & Dannenberg

-and-

Wolkowitz & Beckman

By: _____
(a member of the firm)
Attorneys for Defendant
Martin A. Scott

Reavis & McGrath

By: _____
(a member of the firm)
Attorneys for Defendant
Richard M. Firestone

So ordered:

Nov. 5, 1971

_____
U. S. D. J.

65a

To 81-24

#33

OFFICE RECORD

71 Civ. 2209 (ELP)

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., et al.,

Defendants.

Stipulation

POLLACK & SINGER
61 BROADWAY
NEW YORK, N. Y. 10006
952-0330

ATTORNEYS FOR Allen & Co., Allen & Company, Incorporated Charles Allen, Lee W. Meyers, and Irwin H. Kramer

U. S. DISTRICT COURT
FILED
NOV 24 1971
S. D. OF N. Y.

of the Court of Nov. 5, 1971 Order sheet because counsel for the defendant Lasen-Hall, Herbstein, Herrath & Horwath was not requested to sign the stipulation or given notice that such stipulation would be submitted to the Court pursuant to Rule 41 FRCP

So ordered

Nov. 18, 1971

NOTICE OF SETTLEMENT WITH MEMORANDUM ENDORSED APPROVING SETTLEMENT AND DISMISSAL AND PERMITTING THE BRINGING OF THIRD-PARTY ACTION FILED DECEMBER 13, 1971

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyer, Irwin H. Kramer, Richard M. Firestone, Martin A. Scott, Holtzmann, Wise & Shepard, James W. Deer, Jacobs, Persinger & Parker, and Laventhol, Krekstein, Horwath & Horwath,

Defendants.

71 Civ. 2209 (ELP)

Notice of Settlement

S i r s :

Please take notice that the within is a true copy of a stipulation of dismissal that will be presented for signature to Hon. Edmund L. Palmieri, United States District Judge, at 10:00 o'clock A.M. on December 3, 1971, or as soon thereafter as counsel can be heard in the United States Court House for the Southern District of New York.

Dated: New York, New York
November 30, 1971

Yours, etc.

Pollack & Singer
Attorneys for Defendants
Allen & Company, Incorporated,
Allen & Company,
Charles Allen, Lee W. Meyer,
Irwin H. Kramer
Office & P.O. Address
61 Broadway
New York, New York 10006
(212) 952-0330

To:

Blum, Haimoff, Gerson, Lipson & Szabad, Esqs.
Attorneys for Plaintiff
270 Madison Avenue
New York, New York 10016

Reavis & McGrath, Esqs.
Attorneys for Defendant Richard M. Firestone
1 Chase Manhattan Plaza
New York, New York 10005

Lipper, Keeley, Katcher, Lowey & Dannenberg, Esqs.
Attorneys for Defendant Martin A. Scott
41 East 42nd Street
New York, New York 10017

Holtzmann, Wise & Shepard, Esqs.
Attorneys for Defendants Holtzmann, Wise & Shepard,
James W. Deer, and The Firestone Group, Ltd.
30 Broad Street
New York, New York 10004

D'Amato, Costello & Shea, Esqs.
Attorneys for Defendant Jacobs, Persinger & Parker
116 John Street
New York, New York 10038

Willkie Farr & Gallagher, Esqs.
Attorneys for Defendant Laventhol, Krekstein, Horwath &
Horwath
1 Chase Manhattan Plaza
New York, New York 10005

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyers, Irwin H. Kramer, Richard M. Firestone, Martin A. Scott, Holtzmann, Wise & Shepard, James W. Deer, Jacobs, Persinger & Parker, and Laventhol, Krekstein, Horwath & Horwath,

Defendants.

71 Civ. 2209 (ELP)

Stipulation

---

1. It is stipulated and agreed by and between the plaintiff and all defendants herein that this action be and hereby is dismissed on the merits, with prejudice and without costs, as against all defendants except Laventhol, Krekstein, Horwath & Horwath.

2. It is further stipulated and agreed by and between the plaintiff and all defendants herein, except Laventhol, Krekstein, Horwath & Horwath, that the plaintiff will not seek pre-trial discovery of any kind against any of the said defendants, except Laventhol, Krekstein, Horwath & Horwath, and will not call any of the said defendants, except Laventhol, Krekstein, Horwath & Horwath, as witnesses at the trial, if any, of this action.

3. It is further stipulated and agreed by and between the plaintiff and all defendants herein that the caption of this action shall be amended to delete the names of all defendants except Laventhol, Krekstein, Horwath & Horwath.

Dated: New York, New York
November 30, 1971.

Blum, Haimoff, Gersen, Lipson
& Szabad

By: _____
(a member of the firm)
Attorneys for Plaintiff

Pollack & Singer

By: _____
(a member of the firm)
Attorneys for Defendants
Allen & Company, Incorporated,
Allen & Company,
Charles Allen,
Lee W. Meyer, and Irwin H.
Kramer

Holtzmann, Wise & Shepard

By: _____
(a member of the firm)
Attorneys for Defendants
Holtzmann, Wise & Shepard
James W. Deer and
The Firestone Group, Ltd.

D'Amato, Costello & Shea

By: Richard A. McGuren
(a member of the firm)
Attorneys for Defendant
Jacobs, Persinger & Parker

Lipper, Keeley, Katcher,
Lowey & Dannenberg

-and-

Wolkowitz & Beckman

By: Paul Katcher
(a member of the firm)
Attorneys for Defendant
Martin A. Scott

Reavis & McGrath

By: _____
(a member of the firm)
Attorneys for Defendant
Richard M. Firestone

Willkie Farr & Gallagher

By: _____
(a member of the firm)
Attorneys for Defendant
Laventhol, Krekstein,
Horwath & Horwath

So ordered:

_____
U. S. D. J.

OFFICE RECORD

71a

HERZFELD v. THE FIRESTONE GROUP, LTD., ET AL., 71 Civ. 2209 E.L.P.

DECEMBER 10, 1971:

This settlement between the plaintiff and all the defendants except the Laventhol firm, is hereby approved after argument. Since counsel agree that an amended complaint, which Mr. Haimoff, counsel for plaintiff, expects to serve within 20 days, will set in motion the procedural steps whereby the defendant Laventhol, if it is so advised, can bring third-party actions against any of the settling defendants, there is no unfairness to the objecting defendant Laventhol.

EDMUND L. PALMIERI
U. S. D. J.

LP)

istrict
a
York

eld,

aintiff,

t-

roup, Ltd.,

fendants.

ement

SINGER
DWAY
. Y. 10006
30

Defendants
, Incorpor-
ompany,
Lee W.
Kramer

AFFIDAVIT OF DEFENDANTS ALLEN & CO., INC.: ALLEN & CO.; CHARLES ALLEN; LEE W. MEYER AND IRWIN H. KRAMER IN SUPPORT OF DISMISSAL FILED DECEMBER 15, 1971

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., et al.,

Defendants.

Index No.
71 Civil 2209 (ELP)

Affidavit In Support of Dismissal

State of New York)
: ss.:
County of New York)

Daniel A. Pollack, being duly sworn, deposes and says:

I am a member of the Bar of this Court and a member of the firm of Pollack & Singer, attorneys for five of the 12 defendants in this action: Allen & Company, Incorporated; Allen & Company; Charles Allen; Lee W. Meyer and Irwin H. Kramer.

The stipulation of dismissal entered into between the plaintiff and all defendants other than Laventhol, Krekstein, Horwath & Horwath ("Laventhol") should be "so ordered" unconditionally by this Court -- the belated opposition by Laventhol to the dismissal of other parties, who have settled their differences with the plaintiff, should be overruled and dismissed by this Court.

I
The Nature and Status of the Action

1. The background facts:

The Complaint in this action was filed in the United States District Court for the Southern District of New York on May 18, 1971.

The case was assigned for all purposes to Hon. Edmund L. Palmieri, a member of the pilot program for individual assignment of cases.

The Complaint arose out of the purchase by Gerald L. Herzfeld, the plaintiff, of two units of The Firestone Group, Ltd., a California - based real estate company.

The two units purchased by the plaintiff from The Firestone Group, Ltd. consisted of $500,000.00 in notes and 10,000 shares of stock, for which the plaintiff paid a total of $510,000.00.

The two units were sold to the plaintiff directly by The Firestone Group, Ltd., as part of a private offering by that company -- the total private offering raised $7,500,000.00 and was made to approximately 25 persons, of whom the plaintiff was one.

On or about March 1, 1971, The Firestone Group, Ltd. defaulted on the payment of the notes and an involuntary petition in bankruptcy was filed against the company in the federal court in California.

2. The parties:

The plaintiff at bar, Gerald L. Herzfeld, filed an action in the United States District Court for the Southern District of New York on May 18, 1971.

The Complaint named as defendants the following: The Firestone Group, Ltd. (the seller of the units); Laventhol (the California - based accountants who prepared the financial statements on the basis of which the plaintiff bought his two units); Richard Firestone and Martin Scott (officers of The Firestone Group, Ltd.); Allen & Company, Incorporated (the investment banker that assisted in the private placement); Allen & Company (a partnership which had nothing whatsoever to do with the private placement except that it, too, like the plaintiff, was a purchaser of the units); Charles Allen (a partner of Allen & Company); Irwin Kramer and Lee Meyer (officers of Allen & Company, Incorporated); Holtzmann, Wise & Shepard (a distinguished New York law firm which represented the purchasers of the units); James W. Deer, Esq. (a member of the law firm of Holtzmann, Wise & Shepard); Jacobs, Persinger & Parker (a distinguished New York law firm which represented the seller of the units, The Firestone Group, Ltd.)

3. The Complaint:

The Complaint charged each defendant individually with violations of the federal securities laws -- omissions and misstatements of material facts in connection with the sale by The Firestone Group, Ltd. of the two units to the plaintiff.

4. Separate parties - separate representation:

The various parties defendant were separately represented and each, of course, was free to pursue whatever course he and his counsel deemed appropriate and in his own best interest.

The representation of the parties was as follows:

1. Laventhol - Willkie, Farr & Gallagher
2. Richard M. Firestone - Reavis & McGrath
3. Martin A. Scott - Lipper, Keeley, Katcher, Lowey & Dannenberg
4. Allen & Company, Incorporated (as well as Allen & Company, Charles Allen, Irwin Kramer and Lee W. Meyer, all of whom are associated) - Pollack & Singer
5. Holtzmann, Wise & Shepard (as well as James W. Deer, Esq., a partner) - Holtzmann, Wise & Shepard
6. Jacobs, Persinger & Parker - D'Amato, Costello & Shea

The parties had separate interests and were, at all times, separately represented, as set forth above.

At no time did I, or, to the best of my knowledge, any counsel other than Willkie, Farr & Gallagher, purport to act for Laventhol.

I neither would nor could have acted for Laventhol because my clients believed and still believe, that Laventhol through either negligent or fraudulent accounting work, were the catalytic cause of this lawsuit.

There is no relation whatsoever between my clients and Laventhol, or between my law firm and Willkie, Farr & Gallagher.

My clients determined that they wanted to dispose of this litigation by the plaintiff, and I entered into settlement negotiations to that end with Louis Haimoff, Esq., counsel for the plaintiff.

The law firm of Willkie, Farr & Gallagher was free, at any time, to do the same -- it did not do so for reasons known only to itself, and now seeks to hold captive other parties who have settled their differences with the plaintiff.

If Laventhol or Willkie, Farr & Gallagher suddenly feels alone, that is solely the responsibility of Willkie, Farr & Gallagher -- they are independent counsel and did or should have taken such steps vis-a-vis the plaintiff as they considered necessary and appropriate for their own client.

No lawyer in this action, other than Willkie, Farr & Gallagher speaks for Laventhol, and no lawyer in this action has or had any duty whatsoever to consult with Willkie, Farr & Gallagher on strategy or any other matter -- the whole claim by Willkie, Farr & Gallagher of "clandestine" settlement negotiations is ludicrous: Willkie, Farr & Gallagher was free at any and all times to negotiate settlement with the plaintiff -- it apparently chose not to do so. Similarly, the other defendants were free to negotiate settlement with the plaintiff with or without advising Laventhol or Willkie, Farr & Gallagher. Any claim to the contrary is simply nonsense.

5. The answers:

All parties answered denying liability to the plaintiff.

Laventhol, in its Answer, did not assert any cross-claims against any of the other defendants.

6. The settlement and dismissal of the action by the plaintiff against defendants other than Laventhol:

In order to quiet litigation and to end the matter, various of the defendants entered into settlement negotiations with the plaintiff, and, in or about November, 1971, these defendants, including the five represented by my law firm, settled with the plaintiff, exchanged general releases and

The plaintiff insisted that he be allowed to continue the lawsuit against the remaining defendant, Laventhol, and that insistence was not the concern of the settling defendants.

Due to an inadvertent oversight, the stipulation of dismissal was presented to Judge Palmieri without notice to Laventhol -- since Laventhol was not a settling defendant it did not occur to me that they should receive notice.

Laventhol protested and, on November 23, Judge Palmieri, who had previously "so ordered" the stipulation of dismissal, set it aside, urged counsel to confer and told us that we should re-submit the stipulation of dismissal, this time on notice to Willkie, Farr & Gallagher.

Although, clearly, no meeting of counsel in such a situation is required by any rule either of the Federal Rules of Civil Procedure, or the Rules of the United States District Court for the Southern District of New York, counsel for the settling defendants were quite willing to meet with counsel for Laventhol, as will be detailed below, pp. 13-14. Indeed, since we were all present in the Court at that time, we suggested a meeting forthwith, but counsel for Laventhol, Louis Craco, Esq. of Willkie, Farr & Gallagher refused to meet with us -- evidently, he knew that he had nothing to say to us.

After many attempts to meet with Louis Craco, Esq., including four telephone calls and two letters from me to him, I resubmitted a new stipulation of dismissal, this time on notice to all parties in accord with Rule 41 of the Federal Rules of Civil Procedure.

It is this new and procedurally correct stipulation of dismissal which Willkie, Farr & Gallagher seeks to upset at this time -- their opposition is utterly without merit as a matter of justice, law or equity, and represents nothing more than a vindictive attempt to take unfair advantage of an earlier procedural error which has now been cured.

II

The claimed "prejudice" to Laventhol is illusory

Louis Craco, Esq., on behalf of Laventhol, claims two elements of prejudice from the dismissal -- both are utterly meritless.

The first element of claimed prejudice is that the dismissal "constitutes an attempt to deprive our client of full discovery under the Federal Rules of Civil Procedure" (Craco affidavit, para.3(a)) -- this is sheer nonsense: the stipulation limits the right of the plaintiff, Gerald Herzfeld, to seek discovery against the settling defendants -- it says nothing whatsoever about the rights of Laventhol. Furthermore, Laventhol can seek discovery of the settling defendants as witnesses in this action, or as parties in any third-party action or actions which it might choose to commence.

The second element of claimed prejudice is that the dismissal "would preclude the Court from requiring the settling defendants to contribute to any judgment" (Craco affidavit, para.3(b)) -- this, too, is sheer nonsense: if the settling defendants, who have already bought their peace, are in any way liable to Laventhol for anything the plaintiff may recover against Laventhol, that liability can be established in a third-party action or actions.

The dismissal should be "so ordered" without conditions of any kind.

Laventhol has no vested right, as is shown in the accompanying Memorandum of Law in Support of Dismissal, to have any defendant kept in the case.

If Laventhol really had bona fide claims against the other defendants why did it fail to assert them by way of cross-claims in its Answer?

The reason is simple: the so-called claims are a sour afterthought by Laventhol to prevent others from buying their peace and exposing the vulnerability of Laventhol on the merits of the lawsuit.

Furthermore, not a single evidentiary fact is adduced to show bona fide claims by Laventhol against any of the settling defendants.

If Laventhol still has bona fide claims, or "newly-discovered" bona fide claims against the other defendants why can it not assert them by way of a third-party action or actions, if and when the plaintiff demonstrates that Laventhol is liable to the plaintiff?

The reason is simple: it can, but is afraid to do so because such a third-party action or actions could not withstand a motion or motions for summary judgment.

Again, not a single evidentiary fact is adduced to show bona fide claims by Laventhol against any of the settling defendants.

As to the proposed "conditions" sought by Laventhol, none is warranted or appropriate -- Willkie, Farr & Gallagher are not seeking to protect the rights of Laventhol under the Federal Rules of Civil Procedure, but, rather, they are attempting to expand and enlarge them.

First, Laventhol seeks the right to ammend its Answer within 20 days of the "so ordering" of the stipulation of dismissal -- since the plaintiff is obliged to, and plans to amend his Complaint, Laventhol can simply serve an Answer to the Amended Complaint.

Second, Laventhol seeks the right to serve a third-party complaint on each of the settling defendants, and seeks the right to make service by serving the attorneys -- Laventhol already has, under the Federal Rules of Civil Procedure, the right now or later to serve a third-party complaint or complaints, and there is absolutely no basis for permitting service to be made by any means other than those provided by the Federal Rules of Civil Procedure.

Third, Laventhol seeks the right to have full discovery from every settling defendant as if he or they were still parties to the action -- this is nothing more than an attempt to throw out the Federal Rules of Civil Procedure. If Laventhol makes one or more of the settling

defendants a third-party defendant, it has full rights of discovery -- if not, it has no basis for claiming more than is allowed by the Federal Rules of Civil Procedure, i.e., they may be deposed or discovered as witnesses.

Fourth, Laventhol seeks the tolling of the statute of limitations -- this is absurd and beyond the power of this or any other Court.

The ad hominem statements of Louis Craco, Esq. are both false and irrelevant

As to the unprovoked and vicious ad hominem attack made by Louis Craco, Esq. in his affidavit (para.5) (none of which is relevant to the issue at bar), this Court is respectfully asked to take notice of the following: (1) Louis Craco, Esq. admits that I tried to telephone him on four separate occasions after the last session with the Court, and that I wrote him two letters (copies of which are annexed as Exhibits A and B), all looking to a meeting of counsel; (2) Louis Craco, Esq. admits that in the entire time that elapsed between the last hearing on this matter with this Court (November 23) and the date of this affidavit, (December 9) a period of 16 days, he made only one attempt to return my four calls, and I was out of my office on that one occasion; (3) Louis Craco, Esq. admits that he did not write me a single letter attempting to arrange a meeting of counsel; (4) Louis Craco, Esq. admits that his associate, David, neither telephoned me nor wrote me at any time respecting a meeting of counsel; (5) Louis Craco, Esq. admits that he failed to contact any other counsel to arrange a meeting.

From the foregoing, it is perfectly clear that the one who did not want to meet was Louis Craco, Esq. -- and the reason he did not want to meet was that he knew his position opposing dismissal of this action by the plaintiff against the settling defendants was untenable -- perhaps because his client, Laventhol, did not want to contribute to a settlement, or for some other reason known only to himself.

The scurrilous conduct and papers of Louis Craco, Esq. with their invective and innuendo are mere blinds -- this litigation has been settled by the plaintiff and the defendants other than Laventhol, and that is all there is to the matter.

Conclusion

This Court should "so order" the stipulation of dismissal as it was presented and without conditions of any kind.

Daniel A. Pollack

Sworn to before me this
10th day of December, 1971.

NEIL D. THOMPSON
Notary Public, State of New York
No. 31-9325940
Qualified in New York County
Commission Expires March 30, 1972

November 24, 1971

Louis A. Craco, Esq.
Willkie Farr & Gallagher
1 Chase Manhattan Plaza
New York, New York 10005

Re: Herzfeld v. The Firestone Group, Ltd.

Dear Mr. Craco:

I have tried to reach you twice today by telephone -- the first time I was told that you were on the telephone and would return my call shortly; the second time I was told that you were in conference with your partners and could not be disturbed.

I shall be leaving the office shortly after dictation of this letter and will not be back until Monday.

In view of your apparent inability to take my call or to return my call, it has become exceedingly difficult to fix a time for a meeting and to obtain the consent of all other counsel.

I will try once again Monday morning, but I have no way of knowing the schedules of other counsel.

As I indicated to you, I have Court commitments on Tuesday, Wednesday, Thursday and Friday of next week, so that the only possible day will be Monday.

Very truly yours,

DAP

Daniel A. Pollack

cc: All Counsel

EXHIBIT B - LETTER ANNEXED TO FOREGOING AFFIDAVIT

November 29, 1971

By Hand

Louis A. Craco, Esq.
Willkie Farr & Gallagher
1 Chase Manhattan Plaza
New York, New York 10005

Re: Herrfeld v. The Firestone Group, Ltd. et al.

Dear Mr. Craco:

I tried to reach you by telephone again today, on two separate occasions, one before lunch, and the other after lunch, and was told that you were not available.

As I indicated to you last week, I have Court commitments this week Tuesday, Wednesday, Thursday and Friday in the Southern District, Eastern District, Supreme Court and Eastern District, respectively, and therefore am not able to meet with you on those days.

If you have any interest in pursuing the matter further, and having a conference with all or any counsel, please advise me and I will attempt to arrange a meeting next week.

In accordance with the statement of Judge Palmieri made in Court last week, we are submitting a new stipulation of dismissal signed by all parties and ask you to sign and return the same to us at your early convenience -- also enclosed is a copy for your files.

Very truly yours,

Daniel M. Pollack

Enclosures
cc: All Counsel

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. HERZFELD,

Plaintiff,

-against-

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT, HOLTZMANN, WISE & SHEPARD, JAMES W. DEER, JACOBS, PERSINGER & PARKER, and LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendants.

Index No. 71 Civ. 2209 (ELP)

AFFIDAVIT

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

LOUIS A. CRACO, being duly sworn, deposes and says:

1. I am an attorney at law, duly admitted to the Bar of this Court, and a member of the firm of Willkie Farr & Gallagher, attorneys for the defendant Laventhol, Krekstein, Horwath & Horwath in this action. I am fully familiar with all of the pleadings and prior proceedings herein. I make this affidavit in opposition to the Notice of Settlement and Stipulation which the other parties to this action have submitted through Mr. Pollack of Pollack & Singer for the Court's approval.

2. This action was brought to recover $510,000 in damages for alleged violations of Sections 12(2) and 17(a) of the Securities Act of 1933 and Section 10(b) of the Securities and Exchange Act of 1934, as well as Section 352-c

of the General Business Law of the State of New York. A copy of the summons and complaint which was filed on or about May 18, 1971 is annexed hereto and marked Exhibit 1. Basically, the complaint charges the defendants with having made false and misleading statements to the plaintiff in connection with the purchase by the plaintiff in or about November or December of 1969 of $500,000 of 9-1/4% promissory notes of defendant The Firestone Group, Ltd. and 10,000 shares of common stock of that Company. Although the complaint charges many of the defendants with conduct amounting to gross fraud, it merely alleges that defendant Laventhol, Krekstein, Horwath & Horwath prepared and certified the financial statements of The Firestone Group, Ltd. as of November 30, 1969. Plaintiff charges that this financial statement, when delivered by other defendants to him was inaccurate. Now, after months of clandestine meetings between the plaintiff and the defendants represented by Mr. Pollack of Pollack & Singer (and perhaps other defendants) the existence of which was deliberately hidden from defendant Laventhol, Krekstein, Horwath & Horwath, a settlement has been proposed to the Court whereby all of the defendants except the accountants are to be dropped as parties to this action and relieved of any responsibility to testify as to what they know about the transactions which gave rise to the complaint or to contribute to the satisfaction of any judgment to which plaintiff may be held entitled.

3. The proposed settlement is unfair and prejudicial to our client, the accountants, Laventhol, Krekstein, Horwath & Horwath and against public policy for

the following reasons:

(a) The proposed settlement constitutes an attempt to deprive our client of full discovery under the Federal Rules of Civil Procedure of the very parties who we have reason to believe have information which would totally exonerate our client from claims of wrongdoing against it. This information would not be readily disclosed by the settling defendants because it would prove that they are the ones who are guilty of the wrongdoing which they would have attributed to our client; and

(b) The proposed settlement, insofar as it would preclude the Court from requiring the settling defendants to contribute to any judgment for which our client may be held liable under the federal securities laws constitutes an unlawful effort by the settling parties to defeat the strong policy of the federal securities laws which requires contribution by all parties who are proved to be guilty of a violation as charged.

4. Insofar as the Court may be inclined to approve the proposed settlement despite the foregoing, we hereby request that the Court impose the following terms and conditions on the settlement to provide minimum protection:

(a) Defendant Laventhol, Krekstein, Horwath & Horwath shall have twenty (20) days from the date of service

upon it of the Order of Settlement with Notice of Entry to serve and file an amended answer to the complaint;

(b) Simultaneous with the service of the amended answer of defendant Laventhol, Krekstein, Horwath & Horwath, as above, defendant Laventhol, Krekstein, Horwath & Horwath may serve a third-party complaint on each of the settling defendants, which third-party complaint shall allege against such defendants any claim for wrongdoing in the transactions which gave rise to the original complaint and for which they may be held liable to indemnify defendant Laventhol, Krekstein, Horwath & Horwath or for which they may be held liable to contribute to any judgment which plaintiff may recover. The third-party complaint may be served on each of the defendants by service of a copy of same, together with a copy of the amended answer of defendant Laventhol, Krekstein, Horwath & Horwath, upon each of the attorneys who have appeared for said defendants and need not contain copies of the pleadings heretofore served in this action; and

(c) Insofar as any one or more of the settling defendants is not named a third-party defendant in the third-party complaint, said settling defendant or defendants shall be subject to full discovery by defendant Laventhol, Krekstein, Horwath & Horwath under the Federal Rules of Civil Procedure as if they were parties to this action and the statutes of limitations for such claims as may be asserted against them in an amended third-party complaint shall be tolled.

We believe the foregoing to be just terms and conditions to impose upon the Court's approval of the proposed settlement

as it will make the settling defendants parties to this action as they must be to protect the rights of our client.

5. Unfortunately, I am obliged to draw to the Court's attention certain respects in which Mr. Pollack has conducted himself since our last appearance before this Court. It is necessary to do so, both as a matter of personal and professional privilege and because it bears on the relief which we seek in this application.

Mr. Pollack has provided the Court with copies of letters directed to me which, among other things, state (see his letters of December 1, 1971 and November 24, 1971) that I did not respond to his telephone communications. These statement are not true. I did return his telephone calls at 4 P.M. on November 24, 1971, at which time Mr. Pollack refused to take my call. I recorded this episode in a contemporaneous memorandum, made immediately upon hanging up the phone, a copy of which I can furnish to the Court if Mr. Pollack should choose to put my word in question. Thereafter Mr. Pollack did not again call until November 29, 1971. On that date I was actually engaged before Mr. Justice Suozzi in Nassau County Supreme Court and Mr. Pollack was so informed. He indicated that if I did not call him by a specified hour - which unfortunately was inconsistent with my appearance before the Court - he could not thereafter be reached.

In the lobby of this Courthouse after our last hearing, I told Mr. Pollack that we did indeed desire a meeting of counsel, that we proposed that the meeting be held on Wednesday, December 1, 1971 at a time and place of his choosing and that if he had difficulty reaching me because

of my Court commitments in the intervening days, he could finalize the arrangements with my associate, Mr. Jack David. At no time in any of his telephone conversations did Mr. Pollack ask for Mr. David.

It is not unfair to say, I believe, that Mr. Pollack has never intended to follow the Court's suggestion that counsel for all parties meet to discuss the problems created by the proposed settlement and this is further illustrated by the fact that although Mr. Pollack proposed a meeting during the week of December 6, 1971, he simultaneourly served his notice and stipulation of settlement returnable in this Court on December 3, 1971.

The above is important to set straight the record, now on file in this Court, which is meant to impute to me a disregard of the Court's wishes and professional courtesy; neither imputation is fair or correct.

More to the point Mr. Pollack's behavior in this incident, reflecting the character and energy with which he has attempted to disassociate himself from this lawsuit, illustrates graphically the problems which we may expect to confront us if we were to try to obtain discovery of his clients voluntarily and without the mandate of this Court supported by appropriate sanctions. Mr. Pollack has done nothing in the course of this episode to give us or the Court any reason to believe that suitable accommodations could be worked out for the conduct of discovery of his clients which is necessary for the adequate defense of our client's interests. This fact, we suggest, should be taken into consideration by the Court in determining the propriety

of the terms and conditions which we have proposed above.

WHEREFORE, your deponent respectfully requests that the proposed settlement be disapproved by the Court or, in the alternative, that the terms and conditions set forth in Paragraph 4 herein be imposed upon the parties to the settlement.

Louis A. Graco

Sworn to before me this
8th day of December, 1971.

Rose M. Padula
Notary Public

ROSE M. PADULA
Notary Public, State of New York
No. 41-[illegible]3147
Qualified in Queens County
Certificate filed in New York Co.
Commission Expires March 30, 1973

OFFICE COPY

MEMORANDUM OF DEFENDANT ALLEN AND CO., INC.; ALLEN & CO.; CHARLES ALLEN; LEE W. MEYER AND IRWIN H. KRAMER IN SUPPORT OF DISMISSAL FILED DECEMBER 15, 1971

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., et al.,

Defendants.

Index No.
71 Civil 2209 (ELP)

Memorandum In Support
Of Dismissal

OFFICE COPY

Received 12/10/71
Served
Filed

POLLACK & SINGER
61 BROADWAY, NEW YORK, N.Y. 10006

United States District Court
Southern District of New York

Gerald L. Herzfeld,

Plaintiff,

-against-

The Firestone Group, Ltd., et al.,

Defendants.

Memorandum In Support
of Dismissal

This memorandum is submitted in support of the dismissal of this action by the plaintiff against defendants other than Laventhol, Krekstein, Horwath & Horwath ("Laventhol").

This Court should "so order" the stipulation of dismissal signed by the plaintiff and the defendants other than Laventhol, and submitted to the Court on December 1971 for the reasons stated below.

The pertinent facts are set forth in the affidavit of Daniel A. Pollack, Esq. submitted herewith; for the sake of brevity they will not be repeated here.

I
The Stipulation of Dismissal Should Be So Ordered

The defendants other than Laventhol have fully settled their controversy -- they have bought their peace from the plaintiff. Thus, there is no basis whatsoever for requiring them to remain as parties defendant in this action. Southern Electric Generating Co. v. Allen Bradley Co., 30 F.R.D. 135 (S.D.N.Y. 1962) (Ryan, J.); Broadway & Ninety-Sixth Street Realty Corp. v. Loew's Inc., 23 F.R.D. 9 (S.D.N.Y. 1958) (Dimock, J.)

In the Southern Electric case, supra (30 F.R.D. 135), this Court granted a motion to dismiss a private anti-trust action as to less than all defendants. The plaintiff, who had privately settled with the movants, consented to dismissal. The non-settling defendants objected. The Court stated (at p.136 of 30 F.R.D.):

> "... [N]one of the objecting defendants have a vested right to keep any other defendant in the suit, when plaintiff consents to dismissal. Any possible unfairness in the dismissal of these defendants would seem to be entirely absent.

> Furthermore, under these circumstances, it is patently unfair to compel the plaintiff to sustain the cost of suing these defendants and to compel these defendants to bear the cost and burden of a defense."

Likewise, in the Broadway & Ninety-Sixth St. case, supra (23 F.R.D. 9), the Court dismissed (on consent of the plaintiffs) another private antitrust action as to some of the defendants, over the objection of other defendants, stating (at p.11 of 23 F.R.D.):

> "...I can think of no reason in law or justice why the moving defendants, having bought their peace from plaintiffs, should be required to continue as co-parties with the objecting defendants and for their sole benefit.
>
> The joinder of the moving defendants by plaintiff gave their fellow defendants no vested interest in the presence of the moving defendants as co-parties."

Laventhol cites no authority in support of its opposition to "so ordering" of the stipulation of dismissal. The foregoing authorities are precisely in point and require the dismissal agreed to and sought by the plaintiff and the settling defendants.

* * *

Laventhol attempts to conceal the facts (1) that it has no right to keep the settling defendants in this action and (2) that no prejudice whatsoever will result to it from the settlement, by irrelevant personal invective and misstatement of the provisions of the stipulation and the applicable law.

The so-called "prejudice" to Laventhol (Craco Aff. para. 3(a) and (b)) is totally non-existent for the following reasons:

a] discovery -- The stipulation does not bar discovery of the settling defendants by Laventhol; it only bars such discovery by plaintiff. Laventhol's counsel has simply misstated the stipulation.

To the extent that Laventhol may wish to take such discovery (such as witness depositions after dismissal), the Federal Rules of Civil Procedure afford Laventhol the protection to which it may be entitled.

b] public policy -- Laventhol is itself accused of wilful violations of the federal securities laws, and is a defendant herein; thus Laventhol is hardly an appropriate "private attorney general".

But, even if Laventhol were, such would be no basis for preventing the dismissal here sought. In both the Southern Electric case, supra (30 F.R.D. 135) and Broadway & Ninety-Sixth St. case, supra (23 F.R.D. 9), this Court implicity and expressly rejected Laventhol's arguments. Both of these cases involved alleged violations of the federal antitrust laws, which, even more clearly than the federal securities laws, express and embody a public policy in favor of private enforcement of the statutes there involved and of contribution by those in pari delicto. (See: Perma Life Mufflers v. Intl. Parts, 392 U.S. 134, 138-39 (1968)). Nevertheless, the dismissals there sought were permitted by this Court.

Likewise, any right of indemnity or contribution which Laventhol may have against any of its co-defendants can still be asserted by Laventhol by third-party action following dismissal of this action. (See Rule 14, Fed. R. Civ. P.). If Laventhol really had such a third party claim, it would have already asserted it. It did not do so; and, even on the instant motion, it fails to advise the Court of a single fact creating a basis for such a claim-over by it against any of the settling parties. Obviously, there are no such facts, or such claims-over would have been asserted long before this time.

* * *

The two cases cited by Laventhol are not in point.

Globus Inc. v. Law Research Service, Inc. 318 F. Supp. 955 (S.D.N.Y. 1970) aff'd 442 F.2d 1346 (2d Cir. 1971) had nothing whatever to do with settlements or voluntary dismissal of an action.

The question in Globus was whether the defendant underwriter could claim contribution from its co-defendants after paying a judgment rendered against Blair and them. The Court properly held that it could.

No such question is presented at bar; there has been no trial and no judgment at bar, and to the extent that Laventhol may be entitled to claim-over against its co-defendants, it can still assert such a claim by third-party complaint, after so-ordering of the stipulation at issue at bar. Thus, the stipulation of dismissal at bar poses no threat that defendants will be insulated from claims-over and therefore will not diligently comply with the federal securities laws in the future.

The same is true of de Haas v. Empire Petroleum Company, 286 F. Supp. 809, 815 (D. Col. 1968). The question there was whether the Court should grant summary judgment, dismissing a third-party action that had already been asserted for indemnity and contribution for violation of the federal securities laws. No such third-party action or cross-claims have been filed at bar; nothing in the stipulation of dismissal prevents Laventhol from filing such a third-party claim in the future.

* * *

The failure of Laventhol to serve a cross-claim against its co-defendants in its Answer, or at any other time to date, clearly exposes the baselessness of Laventhol's opposition to the stipulation here at issue. But even had Laventhol asserted such a cross-claim, the existence of the cross-claim would not alter the right of the settling defendants to have the stipulation at bar "so-ordered."

As this Court aptly stated in the Broadway & Ninety-Sixth St. case, supra (23 F.R.D. at pp. 11-12):

> "[I]n suggesting that they will have greater rights to assert a claim for contribution if moving defendants are kept in, objecting defendants in substance say no more than that it will be easier to serve a cross-claim for contribution on existing co-defendants than to get leave to serve a third party complaint for contribution on third parties who have formerly been co-defendants...
>
> Even if the objecting defendants had already served a cross-claim for contribution on the moving defendants, the moving defendants would have been entitled to have the plaintiffs' complaint against them dismissed and they would remain in the case only as third party defendants opposing the objecting defendants' cross-claim." (Emphasis supplied)

The same conclusion is warranted at bar.

Conclusion

The stipulation dismissing this action as to all defendants other than Laventhol should be "so-ordered" unconditionally. The opposition of Laventhol should be overruled.

Respectfully submitted,

Pollack & Singer
Attorneys for Defendants
Allen & Company, Incorporated
Allen & Company,
Charles Allen,
Lee W. Meyer and
Irwin H. Kramer

Of Counsel:

Daniel A. Pollack
Martin I. Kaminsky

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

----------X

GERALD L. HERZFELD,

Plaintiff,

- against -

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendant.

INDEX NO. 71 Civ. 2209

AMENDED COMPLAINT

----------X

Plaintiff, complaining of the defendant, by his attorneys, Blum, Haimoff, Gersen, Lipson & Szabad, alleges (on information and belief except as to Paragraphs 3, 7, 8, 12, 13, 14, 16, 23, 26, 29, 33, 36, 39, and 40):

1. Jurisdiction of this Court over this action is based upon §22(a) of the Securities Act of 1933 (15 U.S.C. §77v[a]) and §27 of the Securities Exchange Act of 1934 (15 U.S.C. §78aa), and upon the principle of pendent jurisdiction.

2. This action arises under §17(a) of the Securities Act of 1933 and §10(b) of the Securities Exchange Act of 1934 and the Rules and Regulations of the Securities & Exchange Commission promulgated thereunder; under §352-c of the General Business Law of the State of New York; and under the common law. The acts of the defendant which are hereinafter alleged took place, unless otherwise indicated, within the Southern District of the State of New York.

3. Plaintiff, GERALD L. HERZFELD is a resident of the

City and County of New York and maintains an office for the transaction of business at 919 Third Avenue, New York, New York.

4. The defendant LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ("Laventhol"), were at all relevant times, and still are, a firm of certified public accountants, duly admitted to practice public accounting in the States of California and New York. Their New York office is located at 919 Third Avenue, New York, New York.

5. At all times relevant herein, The Firestone Group, Ltd. ("Firestone"), was a corporation duly organized under the laws of the State of Delaware, was engaged in the business of the purchase, sale, development and management of real property and interests in real property. The principal offices of the Company are located at 342 North Rodeo Drive, Beverly Hills, California.

6. In or about November and December, 1969, and January, 1970, Firestone solicited the sale of, offered for sale, and sold to purchasers, within the State of New York, in other states of the United States, and in Europe, securities of Firestone, consisting of $7,500,000 of the 9 1/4% promissory notes of Firestone, and 150,000 shares of the common stock of said Company, said securities being offered for sale and sold in Units, each Unit consisting of a note in principal amount of $250,000 and 5,000 shares of the stock at $1 per share.

7. In or about November, 1969, Firestone sold to plaintiff a portion of the securities described in Paragraph 6

hereof, consisting of $500,000 in notes and 10,000 shares of stock, in payment for which plaintiff paid a total of $510,000; the said payment was made at 30 Broad Street, New York, New York, on or about December 6, 1969.

8. The said purchase was made in accordance with Note and Stock Purchase Agreements ("Agreement"), dated November 10, 1969, which were delivered to plaintiff and David Baird ("Baird"), as nominee for plaintiff, by letter dated November 12, 1969, addressed by Firestone to plaintiff and to Baird, stating that "audited financial statements as at and for the 11 months ended November 30, 1969...will be delivered..." at the closing. The said letter stated that "the audited statements will serve as the basis for confirming the unaudited projected financial statements annexed to the Note and Stock Purchase Agreements as Exhibit B".

9. In or about November, 1969, the defendant Laventhol was retained by Firestone to prepare the unaudited financial statements as of November 30, 1969, referred to in said letter of November 12, 1969, copies of which were to be delivered to plaintiff as aforesaid.

10. In or about November, 1969, defendant Laventhol had knowledge, or in the exercise of reasonable care, should have had knowledge, that said audited statements would be delivered by Firestone to plaintiff and would be relied upon by plaintiff in connection with the purchase of the securities hereinabove referred to.

11. Thereafter, and on or about December 6, 1969,

defendant Laventhol completed the preparation of the said audited financial statements and delivered its said report to Firestone, which said report included a certification that the financial statements fairly presented the financial position of Firestone and the results of its operations for the period ended November 30, 1969 in accordance with generally accepted accounting principles, with an exception referred to in said certification. In connection with the preparation of the said audited statements and the delivery of said statements by defendant Laventhol to Firestone and the delivery thereof by Firestone to plaintiff and to other purchasers of said securities, defendant Laventhol employed means and instruments of transportation and communication in inter-state commerce and used the mails in connection therewith, directly and indirectly, as herein alleged and otherwise.

12. On or about December 16, 1969, Firestone delivered to plaintiff copies of the said audited financial statements prepared by said defendant Laventhol as aforesaid. In a letter dated December 16, 1969, accompanying said report, it was stated by Firestone that the financial statements had been "certified by Laventhol, Krekstein, Horwath & Horwath, certified public accountants".

13. In the said letter of December 16, 1969, Firestone advised plaintiff that in the event the differences between the audited financial statements, prepared by defendant Laventhol, and the unaudited statements annexed to the Agreement as Schedule B were determined by plaintiff to be such as would result in a

change of his investment decision, Firestone would refund to plaintiff the payment made by plaintiff for the securities.

14. Plaintiff relied upon the audited financial statements prepared by defendant Laventhol as being truthful and correct and as correctly setting forth Firestone's financial conditions and the result of the operation for the period ended November 30, 1969, and did not take advantage of the offer of rescission made by Firestone as hereinabove alleged.

15. The said consolidated balance sheet, prepared by defendant Laventhol was false and misleading in that said balance sheet reported that Firestone had deferred income of $2,834,133, whereas Firestone had no deferred income and in fact sustained losses in the period ending November 30, 1969.

16. The said consolidated statement of income and a schedule of deferred income, prepared by defendant Laventhol, for the period ending November 30, 1969 was further false and misleading in that it reported:

(a) Sales of $22,132,607.
(b) Gross profit on sales (before deferred gross profit) of $2,317,687.
(c) Deferred gross profit of $1,795,500.
(d) Gross profit on sales, management fees and interest income of $981,579.
(e) Deferred income of $2,834,133.

17. The said statement of income and schedule of deferred income were false and misleading in that:

(a) The sales of $22,132,607 included, among other things, a purported sale of $15,393,000 which sale was never made, as defendant Laventhol knew, or, in the exercise of due care,

should have known.

(b) The gross profit of $2,317,687, and the deferred gross profit of $1,795,500 was false and misleading in that the said purported profit included the sum of $2,030,500, arising out of the said purported sale of $15,393,000, which sale was not, in fact, made, as defendant Laventhol knew, or, in the exercise of due care, should have known.

(c) The income of $981,579 was false and misleading in that said sum was grossly overstated as defendant Laventhol knew, or, in the exercise of due care, should have known.

18. The audited financial statements prepared by defendant Laventhol described in a footnote the terms of the purported sale in the amount of $15,393,000, which description was intended to, and did in fact, convey the impression to plaintiff that the sale had been made, and that the profit of $2,030,500 had in fact been earned, but was being deferred for accounting reasons. In truth and in fact, as defendant Laventhol knew, or, in the exercise of due care, should have known, the said transaction represented an option by Firestone to purchase the property from its former owners and a grant of an option by Firestone to the alleged purchaser to purchase the property. The purchaser from Firestone did not in fact exercise its option to purchase the property from Firestone and Firestone did not exercise its option to purchase the property from the former owners. As of November 30, 1969, defendant Laventhol knew, or, in the exercise of due care, should have known, that no transaction of sale had

been consummated.

19. By reason of the said audited financial statements prepared by defendant Laventhol and delivered to plaintiff, and the false and misleading representations contained in said audited financial statements, plaintiff was not able to exercise an informed judgment as to the offer of rescission made by Firestone.

20. The said financial statements prepared and submitted by defendant Laventhol was further false in that the certificate signed by the defendant Laventhol stated that the financial statements fairly stated the financial position of Firestone and its subsidiaries, in conformity with accepted accounting principles "subject to the collectibility of the balance receivable on the contract of sale (see Note 4 of Note 2 of the financial statement)." The said "balance receivable" was $4,965,250; defendant Laventhol knew or should have known that no such sum was due unless the purchaser elected to consummate the purchase and, in fact, the said transaction was not consummated.

AS AND FOR A FIRST CLAIM

21. This claim is instituted pursuant to §10(b) of the Securities Exchange Act of 1934 (15 U.S.C. §78j) and Rule 10b-5 (17 C.F.R. §240.10b-5) promulgated thereunder for damages resulting from the purchase by plaintiff of said securities, together with the costs of suit and reasonable attorneys' fees, as a result of defendant's violations of the foregoing Act and Rule.

22. Defendant Laventhol, in contravention of §17(a) of the Securities Act of 1933 and §10b of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, aided and abetted and participated in the offer and sale of securities of Firestone by use of means or instrumentalities of interstate commerce or the mails, (a) employed a device, scheme or artifice to defraud plaintiff; (b) made untrue statements of material facts or omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in transactions, practices and a course of business which operated as a fraud and deceit on plaintiff.

23. By reason of the foregoing, plaintiff has been damaged in the amount of $200,000, after deducting sums received by plaintiff in settlement from other persons involved in the sale of the said securities to plaintiff.

AS AND FOR A SECOND CLAIM

24. This action is instituted pursuant to §352-c of the General Business Law of the State of New York.

25. Defendant Laventhol, in contravention of §352-c of the General Business Law of the State of New York, used the following acts or practices to induce or promote the issuance, distribution, exchange, purchase, negotiation and sale of the said securities of Firestone to plaintiff within New York State: (a) fraud, deception, concealment, suppression and false pretense; (b) promises and representations as to the future which were

beyond reasonable expectation and unwarranted by existing circumstances; (c) representations or statements which were false, where defendant (i) knew the truth; (ii) with reasonable effort could have known the truth; or (iii) made no reasonable effort to ascertain the truth; or (iv) did not have knowledge concerning the representations or statements made.

26. By reason of the foregoing, plaintiff has been damaged in the amount of $200,000, after deducting sums received by plaintiff in settlement from other persons involved in the sale of the said securities to plaintiff.

AS AND FOR A THIRD CLAIM

27. The contract entered into between Firestone and Laventhol for the preparation by defendant Laventhol of audited financial statements as of November 30, 1969, was entered into for the benefit of plaintiff and other purchasers of the securities of Firestone.

28. Defendant Laventhol breached the said contract by negligently and carelessly performing the audit and accounting procedures required and by reason of said carelessness and negligence, the audited financial statements prepared by defendant Laventhol and delivered by Firestone to plaintiff were false and misleading.

29. By reason of the breach of contract by defendant Laventhol as aforesaid, plaintiff has been damaged in the sum of $200,000 after deducting sums received by plaintiff in settlement from other persons involved in the sale of the said securities

to plaintiff.

AS AND FOR A FOURTH CLAIM

30. Defendant Laventhol was advised by Firestone that the audited financial statements which defendant Laventhol had contracted to prepare were to be delivered by Firestone to plaintiff for the purpose of providing plaintiff with truthful and correct financial data concerning the assets and liabilities and results of operations of Firestone for the period ending November 30, 1969, and that said financial data would be relied upon by plaintiff in arriving at his decision to retain his investment in the securities of Firestone.

31. By reason of the foregoing, defendant Laventhol had a duty to plaintiff to exercise reasonable care and diligence in the preparation of said financial statements.

32. In violation of said duty, defendant Laventhol negligently and carelessly prepared the said financial statements and negligently and carelessly failed to exercise reasonable care in the preparation of said statements whereby the said statements contained materially false and misleading representations upon which plaintiff relied, to his damage.

33. By reason of the foregoing, plaintiff has been damaged in the amount of $200,000, after deducting sums received by plaintiff in settlement from other persons involved in the sale of the said securities to plaintiff.

AS AND FOR A FIFTH CLAIM

34. When defendant Laventhol entered into a contract

with Firestone to prepare audited financial statements of Firestone for the period ending November 30, 1969, defendant Laventhol knew that said statement would be used by Firestone in connection with the sale of its securities.

35. Defendant Laventhol knew that Firestone's conduct in connection with the sale of its said securities was in violation of law; that Firestone had made false and fraudulent representations to plaintiff in connection with the sale of said securities as herein alleged and otherwise; and that the preparation of the financial statements herein referred to gave substantial assistance to Firestone in connection with the sale of said securities.

36. By reason of the foregoing, plaintiff has been damaged in the amount of $200,000, after deducting sums received by plaintiff in settlement from other persons involved in the sale of the said securities to plaintiff.

AS AND FOR A SIXTH CLAIM

37. When defendant Laventhol entered into a contract with Firestone to prepare audited financial statements of Firestone for the period ending November 30, 1969, defendant Laventhol knew that said statement would be used by Firestone in connection with the sale of its securities.

38. In the preparation of the said financial statements the defendant Laventhol was guilty of fraud, concealment and misrepresentation in that it represented to any prospective purchaser of securities of Firestone that it had adequate

knowledge and data upon the basis of which the financial statements were prepared, whereas, in truth and in fact, said defendant Laventhol had no such adequate knowledge.

39. By reason of the foregoing, plaintiff has been damaged in the amount of $200,000, after deducting sums received by plaintiff in settlement from other persons involved in the sale of the said securities to plaintiff.

40. By reason of the foregoing and without any negligence of the plaintiff contributing thereto, plaintiff has been damaged in the amount of $200,000, after deducting sums received by plaintiff in settlement from other persons involved in the sale of the said securities to plaintiff.

WHEREFORE, plaintiff demands:

1. Judgment in its favor awarding damages due plaintiff in the amount of $200,000 together with interest thereon; and

2. Awarding to plaintiff the costs, disbursements and expenses of this action, including reasonable attorneys' fees and such other and further relief as may be necessary and appropriate.

Louis Haimoff, Of Counsel

BLUM, HAIMOFF, GERSEN, LIPSON & SZABAD
Attorneys for Plaintiff
Office and Post Office Address:
270 Madison Avenue
New York, New York 10016
Tel. No. (212) 683-6383

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. HERZFELD, Plaintiff, -against- LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, Defendant.	71 Civ. 2209 (ELP) ANSWER

Defendant LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ("LKH&H"), by its attorneys, WILLKIE FARR & GALLAGHER, for its answer to the Amended Complaint, alleges the following:

1. Denies each and every allegation contained in paragraph 1 of the Amended Complaint except admits that plaintiff contends that jurisdiction of the Court is based on Section 22(a) of the Securities Act of 1933 (15 U.S.C. Section 77v[a]), Section 27 of the Securities Exchange Act of 1934 (15 U.S.C. Section 78aa) and upon the principle of pendent jurisdiction.

2. Denies each and every allegation contained in paragraph 2 of the Amended Complaint except admits that plaintiff purports to assert claims under Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934 and the Rules and Regulations of the Securities and Exchange Commission promulgated thereunder, and under Section 352-c of the General Business Law of the State of New York and under the common law.

3. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 3 of the Amended Complaint.

4. Admits the allegations contained in paragraph 4 of the Amended Complaint.

5. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 5 of the Amended Complaint.

6. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 6 of the Amended Complaint.

7. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragrpah 7 of the Amended Complaint.

8. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 8 of the Amended Complaint.

9. Denies each and every allegation contained in paragraph 9 of the Amended Complaint except admits that it was retained by THE FIRESTONE GROUP, LTD. ("FIRESTONE") to perform accounting services and further admits that it prepared and issued a report dated December 6, 1969 which expressed an opinion on the audited financial statements of FIRESTONE for the period from December 26, 1968 to November 30, 1969.

10. Denies each and every allegation contained in paragraph 10 of the Amended Complaint.

11. Denies each and every allegation contained in paragraph 11 of the Amended Complaint except admits that on or about December 6, 1969, LKH&H completed and issued a report of that date to FIRESTONE expressing an opinion on certain audited financial statements of FIRESTONE attached thereto, and refers this Court to said report (a copy of which is annexed hereto) for all of the matters contained therein.

12. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 12 of the Amended Complaint.

13. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 13 of the Amended Complaint.

14. Denies knowledge or information sufficient to form a belief as to the truth of each and every allegation contained in paragraph 14 of the Amended Complaint.

15. Denies each and every allegation contained in paragraph 15 of the Amended Complaint and refers this Court to the copy of the report which is annexed hereto for all of the statements contained therein.

16. Denies each and every allegation contained in paragraph 16 of the Amended Complaint and refers this Court to the copy of the report which is annexed hereto for all of the statements contained therein.

17. Denies each and every allegation contained in paragraph 17 of the Amended Complaint.

18. Denies each and every allegation contained in paragraph 18 of the Amended Complaint.

19. Denies each and every allegation contained in paragraph 19 of the Amended Complaint.

20. Denies each and every allegation contained in paragraph 20 of the Amended Complaint and refers this Court to the copy of the report which is annexed hereto for all of the statements contained therein.

21. Denies each and every allegation contained in paragraph 21 of the Amended Complaint except admits that plaintiff purports to assert claims under Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78j) and Rule 10b-5 (17 C.F.R. §240.10b-5) promulgated thereunder.

22. Denies each and every allegation contained in paragraph 22 of the Amended Complaint.

23. Denies each and every allegation contained in paragraph 23 of the Amended Complaint.

24. Denies each and every allegation contained in paragraph 24 of the Amended Complaint except admits that plaintiff purports to assert claims under Section 352-c of the General Business Law of the State of New York.

25. Denies each and every allegation contained in paragraph 25 of the Amended Complaint.

26. Denies each and every allegation contained in paragraph 26 of the Amended Complaint.

27. Denies each and every allegation contained in paragraph 27 of the Amended Complaint.

28. Denies each and every allegation contained in paragraph 28 of the Amended Complaint.

29. Denies each and every allegation contained in paragraph 29 of the Amended Complaint.

30. Denies each and every allegation contained in paragraph 30 of the Amended Complaint.

31. Denies each and every allegation contained in paragraph 31 of the Amended Complaint.

32. Denies each and every allegation contained in paragraph 32 of the Amended Complaint.

33. Denies each and every allegation contained in paragraph 33 of the Amended Complaint.

34. Denies each and every allegation contained in paragraph 34 of the Amended Complaint except admits that it knew that FIRESTONE would use LKH&H's report for normal corporate purposes including the sale of certain of its securities.

35. Denies each and every allegation contained in paragraph 35 of the Amended Complaint insofar as it relates to defendant.

36. Denies each and every allegation contained in paragraph 36 of the Amended Complaint.

37. Denies each and every allegation contained in paragraph 37 of the Amended Complaint.

38. Denies each and every allegation contained in paragraph 38 of the Amended Complaint.

39. Denies each and every allegation contained in paragraph 39 of the Amended Complaint.

40. Denies each and every allegation contained in paragraph 40 of the Amended Complaint.

FOR A FIRST, SEPARATE AND COMPLETE DEFENSE TO THE AMENDED COMPLAINT, DEFENDANT LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ALLEGES:

41. The work done by defendant LKH&H in connection with the issuance of its report dated December 6, 1969, and the report itself were in conformity with generally accepted accounting principles applied on a consistent basis and defendant LKH&H had reasonable ground to believe and did believe, after performing its work in strict compliance with generally accepted auditing standards that the statements in said report were true and accurate.

FOR A SECOND, SEPARATE AND COMPLETE DEFENSE TO THE AMENDED COMPLAINT, DEFENDANT LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ALLEGES:

42. The Amended Complaint fails to state a claim upon which relief can be granted.

FOR A THIRD, SEPARATE AND COMPLETE DEFENSE TO THE AMENDED COMPLAINT, DEFENDANT LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ALLEGES:

43. This Court is without jurisdiction of the subject matter of this action.

FOR A FOURTH, SEPARATE AND COMPLETE DEFENSE TO THE AMENDED COMPLAINT, DEFENDANT LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ALLEGES:

44. The Amended Complaint must be dismissed for improper venue.

WHEREFORE, defendant LAVENTHOL, KREKSTEIN, HORWATH & HORWATH demands judgment dismissing the Amended Complaint, together with the costs and disbursements of this action.

WILLKIE FARR & GALLAGHER
Attorneys for Defendant
Laventhol, Krekstein, Horwath & Horwath

By _____
(A Member of the Firm)
Office & P.O. Address
One Chase Manhattan Plaza
New York, New York 10005

LAVENTHOL KREKSTEIN HORWATH & HORWATH

CERTIFIED PUBLIC ACCOUNTANTS

3700 WILSHIRE BOULEVARD
LOS ANGELES, CALIF. 90005
(213) 381-5393

OFFICES THROUGHOUT THE WORLD

Board of Directors
The Firestone Group, Ltd.
Beverly Hills, California

We have examined the consolidated balance sheet of The Firestone Group, Ltd. and its wholly owned subsidiaries as at November 30, 1969 and the related consolidated statement of income and retained earnings from date of inception on December 26, 1968 to November 30, 1969. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, subject to the collectibility of the balance receivable on the contract of sale (see Note 4 of Notes to Financial Statements), the accompanying consolidated balance sheet and related consolidated statement of income and retained earnings present fairly the financial position of The Firestone Group, Ltd. and its wholly owned subsidiaries as at November 30, 1969 and the results of its operations from date of inception on December 26, 1968 to November 30, 1969, in conformity with generally accepted accounting principles.

Laventhol Krekstein Horwath & Horwath

Certified Public Accountants

December 6, 1969

THE FIRESTONE GROUP, LTD. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET - NOVEMBER 30, 1969

ASSETS

Current assets:		
Cash		$ 41,686
Cash restricted (Note 2)		233,501
Current portion of notes receivable (Note 3)		65,000
Balance receivable on contract of sale (due in January 1970; Note 4)		4,990,250
Deposits on purchase agreements		185,743
Land held for sale (encumbered)		389,567
Prepaid expenses		365,240
Supplies inventory		20,000
Total current assets		6,290,987
Long-term notes receivable (Note 3)	$ 6,739,607.	
Less current portion	65,000	6,674,607
Long-term portion of receivable on contract of sale (Note 4)		1,015,250
Property and equipment, at cost:		
Equipment	84,825.	
Leasehold improvements	1,047.	
	85,872	
Less accumulated depreciation (straight-line method)	6,926.	78,946
Other assets:		
Deferred charges (Note 5)	875,418.	
Deferred income taxes (Note 6)	98,674	
Due from affiliated companies	96,073.	
Other	57,997	
Cash restricted (Note 2)	30,116.	1,158,278
		$ 15,218,068

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Notes payable, banks		$ 932,000
Contract payable (Note 4)		3,995,000
Accounts payable		624,322
Payroll taxes payable		51,324
Income taxes payable		335,437
Total current liabilities		5,938,083
Long-term notes payable (Note 3)		5,761,7
Deferred income (Notes 4 and 7)		2,834,133
Contingent liabilities and commitments (Notes 8 to 12)		[illegible]
Shareholders' equity:		
Preferred stock, par value $1.00 per share; 2,000,000 shares authorized, none issued		
Common stock, par value $0.10 per share; 10,000,000 shares authorized, 666,666 shares issued and outstanding (Note 1)	$ 66,667	
Capital in excess of par value	550,501	
Retained earnings	66,916	684,084
		$ 15,218,068

See notes to financial statements.

FINANCIAL STATEMENTS ANNEXED TO FOREGOING ANSWER

THE FIRESTONE GROUP, LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS

FROM DATE OF INCEPTION ON DECEMBER 26, 1968 TO NOVEMBER 30, 1969

Income:		
Sales		$ 22,132,607
Cost of sales		19,814,920
Gross profit on sales (before deferred gross profit)		2,317,687
Deferred gross profit (Note 4)		1,795,500
Gross profit on sales		522,187
Management fees		240,822
Interest income		218,570
Total income		981,579
Expenses:		
Operating	$ 696,801	
Interest	180,299	877,100
Income before income taxes		104,479
Income taxes:		
Current		136,237
Deferred (Note 6)		(98,674)
Net income		66,916
Retained earnings, beginning		0
Retained earnings, ending		$ 66,916
Earnings per share		0.10

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS ANNEXED TO FOREGOING ANSWER

THE FIRESTONE GROUP, LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOVEMBER 30, 1969

1. The Firestone Group, Ltd. (a Delaware corporation) was incorporated on December 26, 1968. The accompanying financial statements include the accounts of the Company and all of its subsidiaries which are wholly-owned as follows:

Firestone Development Corporation
Firestone Equities Corporation
Firestone Management Corporation
Firestone Securities Corporation
Housing Resources, Inc. (see Note 8)

All material intercompany transactions have been eliminated in the accompanying financial statements.

The Company issued 499,999 shares of its common stock for cash at $1 per share. An additional 166,667 shares were issued for an assignment to The Firestone Group, Ltd. of all of the right, title and interest in three agreements to purchase parcels of real property located in the State of California. These additional shares were valued by the Board of Directors at $1 per share.

The land purchase agreements, which had no cost basis for income tax purposes, were recorded at $366,667, consisting of the value of $166,667 assigned to the common stock exchanged therefor and a liability of $200,000 for the income taxes which would be payable if the agreements were sold for this amount. The real properties underlying the three agreements were subsequently sold for $316,000.

2. An attachment of $30,116 has been filed against the Company's general funds in connection with a suit brought by a former employee. In the opinion of the Company's counsel, the suit is without merit.

Cash held in trust accounts represents interest income received in advance from syndication sales made prior to November 30, 1969. Under the terms of the syndicates' purchase agreements, these funds will become unconditionally available to the Company on January 2, 1970.

3. Long-term notes payable represent encumbrances on properties sold to syndicates on which the Company remains primarily liable. These notes bear interest of from 6.7% to 7.2% per annum. Of the long-term balance due at November 30, 1969 approximately $4,000,000 is payable in instalments through 1981 and the balance is payable in instalments through 1984.

The long-term notes receivable resulting from sales of properties to syndicates (and on which the Company remains obligated for existing first trust deeds) are collateralized by all inclusive trust deeds. These notes mature fifteen years from date of issuance. Provisions for payment require interest only for ten years and annual principal payments sufficient to amortize the notes through maturity.

The Company retains a profit participation of 10% upon the syndicates' reselling the properties in excess of their cost. In general, profit is defined as gross profit less all monies invested by the syndicates and 6% imputed interest thereon.

4. The Firestone Group, Ltd. acquired by contract of sale a group of convalescent hospitals containing approximately 1,900 beds. The properties were leased back to the former owners. In November, 1969 the Company sold the properties by means of a contract of sale.

The terms of the contract by which The Firestone Group, Ltd. purchased the properties provide for the following:

Assumption of existing first trust deed liens	$ 5,822,283
Note payable, secured by second trust deed, requiring monthly amortization of principal and interest at 9-1/4% for 25 years	3,540,217
Cash:	
Upon contract execution	5,000
On December 20, 1969	25,000
On January 30, 1970	3,970,000
	$ 13,362,500

The contract of sale provided for the following:

Assumption of existing trust deed liens	$ 9,362,500
Cash:	
Upon contract execution	25,000
On January 2, 1970	25,00
On January 30, 1970	4,965,250
Note secured by trust deed in favor of The Firestone Group, Ltd. requiring monthly amortization based on twenty-five years with interest of 8-1/2%; final payment due in 120th month	
	1,015,250
	$ 15,393,000

The sales agreement also provides for liquidated damages of $185,000 if the buyer fails to perform.

Of the total gross profit of $2,030,500, $235,000 is included in the consolidated income statement and the balance, $1,795,500 will be considered realized when the January 30. 1970 payment is received. The latter amount is included in deferred income in the consolidated balance sheet.

5. Deferred charges represent costs incurred in connection with research studies related to real estate acquisition in p ocess and for future acquisition and educational seminars which will result in future real estate syndications. These costs are being amortized over the periods which management estimates will benefit therefrom. These periods range from 30 to 36 months.

THE FIRESTONE GROUP, LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
NOVEMBER 30, 1969

6. The deferred income taxes shown under other assets represents, in the main, taxes currently payable on management fees and interest received in advance which are currently reportable for income tax purposes but which are not included as income in the consolidated income statement.

7. The syndications, to which the Company has sold property, prepay interest for a period of two years and generally prepay non-refundable management fees for a period of three years. One third of the management fees are taken into income when received. The balance of such fees together with the prepaid interest is taken into income in the periods to which they apply.

8. An employment contract with a key employee of Housing Resources, Inc. provides that he is to receive 10% of the shares of Housing Resources, Inc. Such stock, may subsequently be exchanged for common stock of The Firestone Group, Ltd. The amount of Firestone Group, Ltd. stock issuable therefor will depend upon the book value of the Housing Resources, Inc. stock and the market value of The Firestone Group, Ltd. stock at the time of exchange. At November 30, 1969, the book value of Housing Resources, Inc. capital stock was nominal.

In addition, the employee will receive an option to acquire 2,500 shares of stock in the Firestone Group, Ltd. at $10 per share.

9. Under the terms of an employment agreement, Mr. Firestone will receive a base annual salary of $60,000 plus a bonus equal to four-tenths of one percent (.004) of the Company's gross income, the bonus not to exceed an aggregate annual amount of $40,000. Mr. Scott's employment agreement provides for a base annual salary of $36,000 plus a bonus equal to twenty-four one hundredths of one percent (.0024) of the gross income of the Company, the bonus not to exceed an aggregate annual amount of $24,000. Maximum bonus has been paid for the period.

10. On January 23, 1969 the Company adopted a qualified stock option plan under which options to purchase 100,000 shares of the Company's common stock were authorized to be granted to certain employees of the Company at no less than 100% of the fair value at date of grant. As of November 30, 1969 no options had been granted under the plan. No charges will be made to income in connection with the options under the plan.

11. The Company has contracted to purchase for syndication thirteen parcels of real estate, including improved and unimproved properties at a cost of $37,449,217. These transactions are expected to close in December 1969 through April 1970.

In December 1969 the Company completed one of the acquisitions at a cost of $2,951,300. At the same time the property was syndicated for $3,043,420. In addition, the Company collected thirty-four months interest income in the amount of $384,978.

In December 1969 the Company received $100,000 in cash and subscriptions of approximately $585,000 toward a required total of $791,000 in connection with another syndication of approximately $3,155,000. The cost of the underlying property is $2,800,000.

12. On November 13, 1969 the Board of Directors approved an arrangement dated November 10, 1969 with Allen & Company Incorporated for the private placement of up to $7,500,000 principal amount of 9-1/2% promissory notes of the Company due December 1, 1975 and up to 150,000 shares of the common stock of The Firestone Group, Ltd. to be sold in units of $250,000 notes and 5,000 shares of common stock at $1 per share or $255,000 per unit. The closing date for the placement is December 16, 1969. The Company will realize $7,450,000 net of fees paid in connection with the placement if the entire issue is placed.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. HERZFELD,

Plaintiff,

-against-

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendant.

71 Civ. 2209

THIRD-PARTY COMPLAINT

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Third-Party Plaintiff,

-against-

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT and DAVID BAIRD,

Third-Party Defendants.

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, third-party plaintiff, by its attorneys, Willkie Farr & Gallagher, for its Third-Party Complaint alleges, upon information and belief:

1. This Court has jurisdiction of this action under Section 22(a) of the Securities Act of 1933 (15 U.S.C. Section 77v[a] and Section 27 of the Securities Exchange Act of 1934 (15 U.S.C. Section 78aa) and the principles of pendent jurisdiction.

2. This action is brought to recover damages which the third-party plaintiff has suffered and may suffer for

which the third-party defendants are and may become liable as a result of violations by the third-party defendants of Sections 17(a) of the Securities Act of 1933 and 10(b) of the Securities Exchange Act of 1934 (First and Second Counts) and as a result of violations by the third-party defendants of common law principles of contract and tort.

3. Acts of each of the third-party defendants took place in the Southern District of New York.

4. Defendant and third-party plaintiff, LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ("LKH&H") is a partnership organized under the laws of the State of Pennsylvania, and a firm of certified public accountants, duly admitted to practice public accounting in the States of California and New York. Its New York office is located at 919 Third Avenue, New York, New York.

5. Third-party defendant THE FIRESTONE GROUP, LTD. ("FIRESTONE") is a corporation organized under the laws of the State of Delaware to conduct a business in the purchase, sale, development and management of real property. The principal offices of Firestone are located at 342 North Rodeo Drive, Beverly Hills, California.

6. Third-Party defendant ALLEN & COMPANY, INCORPORATED ("ALLEN, INC.") was at all relevant times, and still is, a corporation organized under the laws of the State of New York, with a principal place of business at 30 Broad Street, New York, New York. It is engaged primarily in the business of investment banking, underwriting and as a

registered broker dealer in the purchase and sale of various types of securities to the public, both for its own account and for the accounts of others.

7. Third-party defendant ALLEN & COMPANY ("ALLEN CO.") was at all relevant times, and still is, a limited partnership organized and registered under the laws of the State of New York, with a principal place of business at 30 Broad Street, New York, New York. It is engaged primarily in the business of investment banking, underwriting and as a registered broker dealer in the purchase and sale of various types of securities to the public both for its own account and for the accounts of others.

8. Third-party defendant CHARLES ALLEN was at all relevant times, and still is, a General Partner of ALLEN CO., an Officer and Director of ALLEN, INC. and a major stockholder and controlling person of FIRESTONE.

9. Third-party defendant LEE W. MEYERS was, at all relevant times, a Vice President of ALLEN, INC. and at all relevant times and until December, 1970, was a Director of FIRESTONE.

10. Third-party defendant IRWIN H. KRAMER was, at all relevant times, a Vice President of ALLEN, INC.

11. Third-party defendant RICHARD M. FIRESTONE was at all relevant times, President and a Director of FIRESTONE.

12. Third-party defendant MARTIN A. SCOTT was at all relevant times a Vice President and Director of FIRESTONE.

13. Third-party defendant DAVID BAIRD was at all relevant times a broker dealer engaged in the purchase and sale of securities, with a principal place of business at 67 Broad Street, New York, New York.

14. LKH&H was retained by FIRESTONE, pursuant to an agreement, to examine and prepare a report on the financial statements of FIRESTONE for the period from December 26 to November 30, 1969.

15. On or about December 6, 1969, LKH&H completed and issued a report of that date to FIRESTONE which report stated that its examination of the financial statements of FIRESTONE "was made in accordance with generally accepted auditing standards." In the same report, LKH&H stated that

> "in our opinion, subject to the collectibility of the balance receivable on the contract of sale (see Note 4 of Notes to Financial Statements), the accompanying consolidated balance sheet and related consolidated statement of income and retained earnings present fairly the financial position of The Firestone Group, Ltd. and its wholly owned subsidiaries as at November 30, 1969 and the results of its operations from date of inception on December 26, 1968 to November 30, 1969, in conformity with generally accepted accounting principles."

16. Plaintiff GERALD L. HERZFELD ("HERZFELD") on May 20, 1971 filed a complaint against third-party defendants hereinabove named (except DAVID BAIRD) and against defendant LKH&H. The complaint charged that each of the third-party defendants (except DAVID BAIRD) hereinabove

named, who were defendants in that action, had defrauded the plaintiff through acts and representations in violation of Section 10(b) of the Securities Exchange Act of 1934, Section 17 of the Securities Act of 1933 and Section 352-c of the General Business Law of the State of New York and other common law principles as follows:

(a) Third-party defendants solicited the sale of, offered for sale, and sold to the public, within the State of New York, in other states of the United States, and in Europe, unregistered securities of FIRESTONE consisting of $7,500,000 of the 9-1/4% promissory notes of FIRESTONE and 150,000 shares of the common stock of FIRESTONE, said securities being offered for sale and sold in Units, each Unit consisting of a note in principal amount of $250,000, and 5,000 shares of the stock at $1.00 per share;

(b) Third-party defendants sold to plaintiff a portion of the securities described in subparagraph (a), consisting of $500,000 in notes and 10,000 shares of stock in payment for which plaintiff paid a total of $510,000. The sale to plaintiff was accomplished by use of means or instruments of transportation and communication in interstate commerce and use of the mails in connection therewith, directly and indirectly;

(c) In connection with the sale to plaintiff, CHARLES ALLEN communicated to plaintiff, through DAVID BAIRD, acting as agent for third-party defendants, and DAVID BAIRD communicated to plaintiff the following untrue and misleading statement of material fact: that the securities of FIRESTONE were "the hottest thing ALLEN ever had." IRWIN H. KRAMER communicated to plaintiff that the FIRESTONE securities were "the best thing ALLEN ever had;"

(d) Beginning on or about November 12, 1969, and from time to time thereafter, third-party defendants communicated to plaintiff, expressly and by implication, the following untrue statements and omissions of material fact:

(i) that financial statements given by third-party defendants to plaintiff prior to December 6, 1969 were certified by LKH&H when, in fact, they had not been certified by LKH&H, and that such financial statements given by third-party defendants to plaintiff subsequent to December 6, 1969 and alleged to have been certified by LKH&H reported gross sales for the period ended November 30, 1969, which included $15.3 million dollars for a sale which was never consummated and also reported fictitious profits of $2,030,500 of current and deferred income;

(ii) that financial statements given by third-party defendants to plaintiff reported projected earnings for the 12 months ending December 31, 1969 of more than $3 million dollars, whereas, in fact, there were little or no earnings during that period;

(iii) that the issuance and sale of the Units were exempt from the Registration and Prospectus requirements of the Securities Act of 1933, as a transaction not involving a public offering; whereas, in fact, the issuance and the sale of the said Units were subject to the Registration and Prospectus requirements of the Securities Act of 1933;

(e) On or about December 16, 1969, FIRESTONE communicated by letter to plaintiff the following further false statements of material facts:

(i) Prepaid interest and prepaid management fees were adjusted upward from the amounts projected;

(ii) Sales and costs of sales increased from the amounts projected and net income was lower than projected, principally as a result of changes in closing schedules;

(iii) Net income for the period ended November 30, 1969 is shown on the audited statement as $66,916 as against $315,000 projected. The transactions originally scheduled to close in November will now close in December which will make up the difference in current net income between that projected and the actual. Deferred income

shown on the audited balance sheet has been increased to $2,834,133 as against $1,421,000 projected. The differential between the net worth shown on the projected balance sheet and the net shown on the audited balance sheet is almost entirely attributable to the reclassification of income from a current basis to a deferred basis;

(iv) The rescheduling by the Company of its closings as aforesaid has resulted in a decrease in the assets of the Company with a corresponding decrease in liabilities from those projected;

(v) We believe that none of these changes have resulted or will result in an adverse change in our financial condition or the results of our operations.

These representations were untrue and created the false impression that FIRESTONE had earned approximately $3 million dollars in 1969; that changes between the unaudited statements and the audited statements were of a technical nature; and that the current and deferred income reflected actual operating profits, whereas, in fact, FIRESTONE had earned little or no profit in 1969.

The complaint charged that LKH&H had also defrauded plaintiff by reason of the alleged misrepresentations contained in the Firestone financial statements attached to the December 6, 1969 report of LKH&H which financial statements and report were delivered to plaintiff by third-party defendants.

17. After plaintiff and third-party defendants (other than BAIRD) settled the plaintiff's claims against them for $300,000, plaintiff filed an Amended Complaint naming LKH&H as defendant. A copy of the Amended Complaint is attached hereto as Exhibit A. In the Amended Complaint, plaintiff alleges that the report issued by LKH&H on December 6, 1969 and the financial statements attached thereto were delivered by FIRESTONE to plaintiff and were relied upon

by plaintiff in connection with the purchase of the securities hereinabove referred to and that these financial statements contained information that was false and misleading and that the report was also, therefore, false and misleading. The Amended Complaint charges that LKH&H is, therefore, liable to plaintiff for violations of Section 10(b) of the Securities Exchange Act of 1934, Section 17 of the Securities Act of 1933 and Section 352-c of the General Business Law of the State of New York and other common law principles.

FIRST COUNT

18. This Court has jurisdiction of this claim under Section 22(a) of the Securities Act of 1933 and Section 27 of the Securities Exchange Act of 1934.

19. Repeats and realleges each and every allegation contained in paragraphs 3 through 17 of this Third-Party Complaint with the same force and effect as if herein fully set forth.

20. Repeats and realleges each and every allegation contained in subparagraphs (a), (b), (c) and (e) of paragraph 16 with the same force and effect as if herein fully set forth and avers that each of the acts and statements described in said subparagraphs was done by the third-party defendants.

21. The third-party defendants made or supplied representations in the books and records of FIRESTONE and made oral and written representations to LKH&H which constituted false and misleading statements and omissions of material fact. In particular, FIRESTONE, RICHARD M. FIRESTONE and MARTIN A. SCOTT made specific representations concerning the financial statements of FIRESTONE in a letter sent to LKH&H at or about the date on which LKH&H issued its report, stating therein that FIRESTONE's receivables were collectible in their entirety and that all liabilities of FIRESTONE had been disclosed to LKH&H. Further, RICHARD M. FIRESTONE, MARTIN A. SCOTT and FIRESTONE represented as accurate the information and opinions which they previously expressed to LKH&H in connection with the audit by LKH&H of FIRESTONE's financial statements, and said that "receivables (of FIRESTONE)...are all deemed collectible in their entirety" and that "all liabilities of the company... have been recorded or have been disclosed to you." These statements also constituted false and misleading statements and omissions of material fact. By their statements, each of the third-party defendants have perpetrated a device, scheme or artifice to defraud LKH&H and the plaintiff and have engaged in transactions, practices or courses of business which operated as a fraud or deceit upon LKH&H and upon the plaintiff.

22. Each third-party defendant, through the means and instrumentalities of interstate commerce and by the mails, failed in its duty to disclose to the plaintiff

and to LKH&H material information which each such third-party defendant knew or should have known and/or made representations to the plaintiff and to LKH&H which constituted false and misleading statements and omissions of material fact.

23. The false and misleading representations made by third-party defendants to LKH&H were consistent with and corroborative of LKH&H's findings upon its examination of the Firestone financial statements and to that extent, were justifiably relied upon by LKH&H in issuing the report dated December 6, 1969 to which reference is made in paragraph 15 herein.

24. LKH&H has and is incurring substantial expense in this action and may be found liable to the plaintiff solely because of the false and misleading written and oral representations given and made to plaintiff and to LKH&H by third-party defendants and each of them, in violation of Section 17(a) of the Securities Act of 1933 and Section 10(b) of the Securities and Exchange Act of 1934.

25. The third-party defendants are liable to LKH&H for the costs, expenses and attorney's fees that LKH&H is sustaining and will sustain in this action and, if judgment is recovered by the plaintiff from LKH&H, the third-party defendants shall be liable to LKH&H in an amount equal to any judgment that may be recovered by plaintiff from LKH&H.

SECOND COUNT

26. This Court has jurisdiction of this claim under Section 22(a) of the Securities Act of 1933 and Section 27 of the Securities Exchange Act of 1934.

27. Repeats and realleges each and every allegation contained in paragraphs 3 through 17, 20 through 23 of this Third-Party Complaint with the same force and effect as if herein fully set forth.

28. If judgment is rendered for the plaintiff and against LKH&H, then each third-party defendant actively and fraudulently participated in the wrongdoing of which plaintiff complains.

29. The third-party plaintiff LKH&H is entitled to contribution from each such third-party defendant for any judgment that may be recovered by plaintiff from LKH&H.

THIRD COUNT

30. This Court has jurisdiction of this claim under the principles of pendent jurisdiction.

31. Repeats and realleges each and every allegation contained in paragraphs 3 through 17 and 20 through 23 of this Third-Party Complaint with the same force and effect as if herein fully set forth.

32. LKH&H has been damaged by the wrongful conduct of each third-party defendant and LKH&H demands judgment over against each such third-party defendant in an

amount equal to any judgment that may be recovered by plaintiff from LKH&H.

FOURTH COUNT

33. This Court has jurisdiction of this claim under the principles of pendent jurisdiction.

34. Repeats and realleges each and every allegation contained in paragraphs 3 through 17 and 20 through 23 of this Third-Party Complaint with the same force and effect as if herein fully set forth.

35. If judgment for the plaintiff is rendered on the claims set forth in the Amended Complaint, then FIRESTONE beached its warranty to LKH&H that the information contained in the financial statements and otherwise given to LKH&H was accurate which was part and parcel of FIRESTONE's engagement of LKH&H to perform auditing and accounting services.

36. FIRESTONE is liable to LKH&H in an amount equal to any judgment that may be recovered by plaintiff from LKH&H and for the costs, expenses and attorney's fees incurred and to be incurred by LKH&H in this action.

WHEREFORE, the third-party plaintiff, LKH&H, demands judgment against the third-party defendants and each of them as follows:

1. On the First Count herein, the attorney's fees, costs and expenses of this action together with any amount which the plaintiff may recover against LKH&H;

2. On the Second Count, contribution from each of the third-party defendants for any amount which plaintiff may recover against LKH&H;

3. On the Third Count, any amount which the plaintiff may recover against LKH&H; and

4. On the Fourth Count, any amount equal to any judgment which plaintiff may recover against LKH&H together with the costs, expenses and attorney's fees of LKH&H in this action,

and for such other relief as this Court deems just.

WILLKIE FARR & GALLAGHER
Attorneys for Third-Party
Plaintiff, LAVENTHOL, KREKSTEIN,
HORWATH & HORWATH

By _____
(A Member of the Firm)

Office & P. O. Address
One Chase Manhattan Plaza
New York, New York 10005

ANSWERS AND COUNTERCLAIMS OF THIRD-PARTY DEFENDANTS THE FIRESTONE GROUP, LTD.; ALLEN & CO., INC.; ALLEN & CO.; CHARLES ALLEN; LEE W. MEYER AND IRWIN H. KRAMER FILED FEBRUARY 29, 1972

United States District Court
Southern District of New York

Gerald L. Herzfeld, Plaintiff, -against- Laventhol, Krekstein, Horwath & Horwath, Defendant.	71 Civ. 2209 (ELP)
Laventhol, Krekstein, Horwath & Horwath, Third-Party Plaintiff, -against- The Firestone Group, Ltd., Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyer, Irwin H. Kramer, Richard M. Firestone, Martin A. Scott and David Baird, Third-Party Defendants.	

Answers and Counterclaims
of Third-Party Defendants

Third-Party Defendants, Allen & Company, Incorporated ("Allen, Inc."), Allen & Company ("Allen Co."), Charles Allen, Irwin H. Kramer deny each and every allegation of the Third-Party Complaint except as expressly admitted or otherwise specifically denied, as follows:

Paragraph	Specific Response
4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 16	Admit.

First Affirmative Defense

1. The Third-Party Complaint fails to state claims upon which relief may be granted.

Second Affirmative Defense

2. Third-Party Plaintiff, Laventhol, Krekstein, Horwath & Horwath ("Laventhol") is estopped and barred by its own conduct from raising the claims alleged in the Third-Party Complaint.

Third Affirmative Defense and
First Counterclaim of
Allen Co. and Allen Inc.
Against Laventhol

1. Jurisdiction of this Court over these counterclaims is based upon Sec. 22(a) of the Securities Act of 1933 (15 U.S.C. Sec, 77v(a)) and Sec. 27 of the Securities Exchange Act of 1934 (15 U.S.C. Sec. 78aa), and upon the principle of pendent jurisdiction.

2. These counterclaims arise under Sec. 17(a) of the Securities Act of 1933 and Sec. 10(b) of the Securities Act of 1934 and the Rules and Regulations of the Securities & Exchange Commission promulgated thereunder, under Sec. 352-c of the General Business Law of

the State of New York, and under the common law. The acts of the Laventhol which are hereinafter alleged took place, unless otherwise indicated, within the Southern District of the State of New York.

3. Third-Party Defendant, Allen Co. was at all relevant times, and still is, a limited partnership organized and registered under the laws of the State of New York, with a principal place of business at 30 Broad Street, New York, New York. It is engaged primarily in the business of investment banking, underwriting and as a registered broker dealer in the purchase and sale of various types of securities to the public both for its own account and for the accounts of others.

4. Third-Party Defendant, Allen Inc., was at all relevant times, and still is, a corporation organized under the laws of the State of New York, with a principal place of business at 30 Broad Street, New York, New York. It is engaged primarily in the business of investment banking, underwriting and as a registered broker dealer in the purchase and sale of various types of securities to the public, both for its own account and for the accounts of others.

5. Allen Co. and Allen Inc. are the owners of preferred stock in Firestone, obtained in exchange for Notes of Firestone purchased by Allen Co. and Allen Inc.

from various persons who purchased same from Firestone as more fully described hereinafter, and are the assignees of all rights of the purchasers ("the Purchasers").

6. Laventhol was at all relevant times, and still is a firm of certified public accountants, duly admitted to practice public accounting in the States of California and New York. Their New York office is located at 919 Third Avenue, New York, New York.

7. At all times relevant herein, The Firestone Group, Ltd. ("Firestone"), was a corporation duly organized under the laws of the State of Delaware, was engaged in the business of the purchase, sale, development and management of real property and interests in real property. The principal offices of the Company are located at 342 North Rodeo Drive, Beverly Hills, California.

8. In or about November and December, 1969, and January, 1970, Firestone solicited the sale of, offered for sale, and sold to purchasers, within the State of New York, in other states of the United States, and in Europe, securities of Firestone, consisting of $7,500,000 of the 9 1/4% promissory notes of Firestone, and 150,000 shares of the common stock of said Company, said securities being offered for sale and sold in Units, each Unit consisting of a note in principal amount of $250,000 and 5,000 shares of the stock of $1 per share.

9. In or about November, 1969, Firestone sold to the Purchasers a portion of the securities described in Paragraph 8 hereof, consisting of four and one half (4 1/2) of the aforesaid Units of notes and stock of Firestone in payment for which Firestone was paid a total of $1,147,500.00 purchased by Allen Co., and three and three tenths (3 3/10) of the aforesaid Units of notes and stock of Firestone in payment for which Firestone was paid a total of $742,500.00 purchased by Allen Inc. The said payments were made at 30 Broad Street, New York, New York on or about December 6, 1969.

10. The said purchases were made in accordance with Note and Stock Purchase Agreements ("Agreement"), dated November 10, 1969, which were delivered to the Purchasers, by letter dated November 12, 1969, addressed by Firestone to the Purchasers, stating that "audited financial statements as at and for the 11 months ended November 30, 1969...will be delivered..." at the closing. The said letter stated that "the audited statements will serve as the basis for confirming the unaudited projected financial statements annexed to the Note and Stock Purchase Agreements as Exhibit B"

11. In or about November, 1969, Laventhol was retained by Firestone to prepare the unaudited financial statements as of November 30 1969, referred to in said letter of November 12, 1969, copies of which were to be delivered to the Purchasers as aforesaid.

12. In or about November, 1969, Laventhol had knowledge, or in the exercise of reasonable care, should have had knowledge, that said audited statements would be delivered by Firestone to the Purchasers and would be relied upon the Purchasers in connection with the purchases of the securities hereinabove referred to.

13. Thereafter, and on or about December 6, 1969, Laventhol completed the preparation of the said audited financial statements and delivered its said report to Firestone, which said report included a certification that the financial statements fairly presented the financial position of Firestone and the results of its operations for the period ended November 30, 1969 in accordance with generally accepted accounting principles, with an exception referred to in said certification. In connection with the preparation of the said audited statements and the delivery of said statements by Laventhol to Firestone and the delivery thereof by Firestone to the Purchasers of said securities, Laventhol employed means and instruments of transportation and communication in inter-state commerce and used the mails in connection therewith, directly and indirectly, as herein alleged and otherwise.

14. On or about December 16, 1969, Firestone delivered to the Purchasers copies of the said audited financial statements prepared by Laventhol as aforesaid.

In a letter dated December 16, 1969, accompanying said report, it was stated by Firestone that the financial statements had been "certified by Laventhol, Krekstein, Horwath & Horwath, certified public accountants".

15. In the said letter of December 16, 1969, Firestone advised the Purchasers that in the event the differences between the audited financial statements, prepared by Laventhol, and the unaudited statements annexed to the Agreement as Schedule B were determined by the Purchasers to be such as would result in a change of their investment decision, Firestone would refund to the Purchasers the payments made by the Purchasers for the securities.

16. The Purchasers relied upon the audited financial statements prepared by Laventhol as being truthful and correct and as correctly setting forth Firestone's financial condition and the result of its operations for the period ended November 30, 1969, and did not take advantage of the offer of rescission made by Firestone as hereinabove alleged.

17. The said consolidated balance sheet, prepared by Laventhol was false and misleading in that said balance sheet reported that Firestone had deferred income of $2,834,133, whereas Firestone had no deferred income and in fact sustained losses in the period ending November 30, 1969.

18. The said consolidated statement of income and a schedule of deferred income, prepared by Laventhol, for the period ending November 30, 1969 was further false and misleading in that it reported:

(a) sales of $22,132,607;

(b) gross profit on sales (before deferred gross profit) of $2,317,687;

(c) deferred gross profit of $1,795,500;

(d) gross profit on sales, management fees and interest income of $981,579;

(e) deferred income of $2,834,133.

19. The said statement of income and schedule of deferred income were false and misleading in that:

(a) the sales of $22,132,607 included, among other things, a purported sale of $15,393,000 which sale was never made, as Laventhol knew or, in the exercise of due care, should have know;

(b) the gross profit of $2,317,687, and the deferred gross profit of $1,795,500 was false and misleading in that the said purported profit included the sum of $2,030,500, arising out of the said purported sale of $15,393,000, which sale was not, in fact, made, as Laventhol knew or, in the exercise of due care, should have known;

(c) the income of $981,579 was false and misleading in that said sum was grossly overstated as Laventhol knew or, in the exercise of due care, should have known.

20. The audited financial statements prepared by Laventhol described in a footnote the terms of the purported sale in the amount of $15,393,000, which description was intended to, and did in fact, convey the impression to the Purchasers that the sale had been made, and that the profit of $2,030,500 had in fact been earned, but was being deferred for accounting reasons. In truth and in fact, as Laventhol knew or, in the exercise of due care, should have known, the said transaction represented an option by Firestone to purchase the property from its former owners and a grant of an option by Firestone to the alleged purchaser to purchase the property. The purchaser from Firestone did not in fact exercise its option to purchase the property from Firestone and Firestone did not exercise its option to purchase the property from the former owners. As of November 30, 1969, Laventhol knew or, in the exercise of due care, should have known, that no transaction of sale had been consummated.

21. By reason of the said audited financial statements prepared by Laventhol and delivered to the purchasers, and the false and misleading representations contained in said audited financial statements, the Purchasers were not able to exercise an informed judgment as to the offer of rescission made by Firestone.

22. The said financial statements prepared and submitted by Laventhol were further false in that the

certificate signed by the Laventhol stated that the financial statements fairly stated the financial position of Firestone and its subsidiaries, in conformity with accepted accounting principles "subject to the collectibility of the balance receivable on the contract of sale (see Note 4 of Note 2 of the financial statement)". The said "balance receivable" was $4,965,250; Laventhol knew or should have known that no such sum was due unless the Purchaser elected to consummate the purchase and, in fact, the said transaction was not consummated.

23. By reason of the foregoing, Laventhol, in contravention of Sec. 17(a) of the Securities Act of 1933 and Sec. 10b of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, aided and abetted and participated in the offer and sale of securities of Firestone by use of means or instrumentalities of interstate commerce or the mails, (a) employed a device, scheme or artifice to defraud the Purchasers; (b) made untrue statements of material facts or omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in transactions, practices and a course of business which operated as a fraud and deceit on the Purchasers.

24. By reason of the foregoing, Allen Co. and Allen Inc. have been damaged by Laventhol in the amount of $1,890,000.00.

Fourth Affirmative Defense and
Second Counterclaim of
Allen Co. and Allen Inc.
Against Laventhol

25. Allen Co. and Allen Inc. repeat and reallege paragraphs 1 through 22 hereinabove.

26. By reason of the foregoing, Laventhol, in contravention of Sec. 352-c of the General Business Law of the State of New York, used the following acts or practices to induce or promote the issuance, distribution, exchange, purchase, negotiation and sale of the said securities of Firestone to the Purchasers within New York State: (a) fraud, deception, concealment, suppression and false pretense; (b) promises and representations as to the future which were beyond reasonable expectation and unwarranted by existing circumstances; (c) representations or statements which were false, where Laventhol (i) knew the truth; (ii) with reasonable effort could have known the truth; or (iii) made no reasonable effort to ascertain the truth; or (iv) did not have knowledge concerning the representations or statements made.

27. By reason of the foregoing, Allen Co. and Allen Inc. have been damaged by Laventhol in the amount of $1,890,000.00.

Fifth Affirmative Defense and
Third Counterclaim of
Allen Co. and Allen Inc.
Against Laventhol

28. Allen Co. and Allen Inc. repeat paragraphs 1 -22 hereinabove.

29. The contract entered into between Firestone and Laventhol for the preparation by Laventhol of audited financial statements as of November 30, 1969, was entered into for the benefit of the Purchasers and other purchasers of the securities of Firestone.

30. Laventhol breached the said contract by negligently and carelessly performing the audit and accounting procedures required and by reason of said carelessness and negligence, the audited financial statements prepared by Laventhol and delivered by Firestone to plaintiff were false and misleading.

31. By reason of the breach of contract by Laventhol as aforesaid, Allen Co. and Allen Inc. have been damaged in the sum of $1,890,000.00.

Sixth Affirmative Defense and
Fourth Counterclaim of
Allen Co. and Allen Inc.
Against Laventhol

32. Allen Co. and Allen Inc. repeat paragraphs 1 -22, 29 and 30 hereinabove.

33. Laventhol was advised by Firestone that the audited financial statements which Laventhol had contracted

to prepare were to be delivered by Firestone to the Purchasers for the purpose of providing the Purchasers with truthful and correct financial data concerning the assets and liabilities and results of operations of Firestone for the period ending November 30, 1969, and that said financial data would be relied upon by the Purchasers in arriving at their decision to retain their investments in the securities of Firestone.

34. By reason of the foregoing, Laventhol had a duty to the Purchasers to exercise reasonable care and diligence in the preparation of said financial statements.

35. In violation of said duty, Laventhol recklessly, negligently and carelessly prepared the said financial statements and failed to exercise reasonable care in the preparation of said statements whereby the said statements contained materially false and misleading representations upon which the Purchasers relied, to their damage.

36. By reason of the foregoing, Allen Co and Allen Inc. have been damaged in the amount of $1,890,000.00.

Sixth Affirmative Defense and
Fifth Counterclaim of
Allen Co. and Allen Inc.
Against Laventhol

37. Allen Co. and Allen Inc. repeat paragraphs 1-22, 29, 30 and 33-35 hereinabove.

38. When Laventhol entered into its contract with Firestone to prepare audited financial statements of Firestone for the period ending November 30, 1969, Laventhol knew that said statement would be used by Firestone in connection with the sale of its securities.

39. Laventhol knew that Firestone's conduct in connection with the sale of its said securities was in violation of law and that Firestone had made false and fraudulent representations to the Purchasers in connection with the sales of said securities as herein alleged and otherwise.

40. Laventhol further knew and intended that the preparation of the financial statements herein referred to gave substantial assistance to Firestone in connection with the sales of said securities.

41. By reason of the foregoing, Allen Co. and Allen Inc. have been damaged in the amount of $1,890,000.00.

Seventh Affirmative Defense and
Sixth Counterclaim of
Allen Co. and Allen Inc.
Against Laventhol

42. Allen Co. and Allen Inc. repeat paragraphs 1-22, 29, 30, 33-35, and 38-40 hereinabove.

43. In the preparation of the said financial statements of Firestone, Laventhol was guilty of fraud,

concealment and misrepresentation in that it represented to any prospective purchaser of securities of Firestone that it had adequate knowledge and data upon the basis of which the financial statements were prepared, whereas, in truth and in fact, Laventhol had no such adequate knowledge.

44. The aforesaid misrepresentations and omissions were knowingly and intentionally made by Laventhol with intent to deceive the public and to induce the Purchasers, among others, to believe that Laventhol had such adequate knowledge, and to rely and to act in reliance therein. The Purchasers did so believe and rely and act in reliance thereon to their detriment and damage.

45. By reason of the foregoing and without any negligence of the Purchasers contributing thereto, Allen Co. and Allen Inc. have been damaged in the amount of $1,890,000.00.

Wherefore, Third-Party Defendants, Allen Co. and Allen Inc., Charles Allen, Irwin H. Kramer demand judgment in their favor as follows:

1. dismissing the Third-Party Complaint;

2. awarding to Allen Co. and Allen Inc. and assessing against Laventhol damages in the amount of $1,890,000.00 together with interest thereon;

3. awarding to them the costs, disbursements and expenses of this action, including reasonable attorneys' fees;

4. granting them such other and further relief as the Court may be deem owing and proper.

Pollack & Singer

By: _____
(a member of the firm)
Attorneys for Third-Party
Defendants
Allen & Company, Incorporated,
Allen & Company, Charles Allen,
Irwin H. Kramer
Office & P.O. Address
61 Broadway
New York, New York 10006
(212) 952-0330

REPLY OF DEFENDANT/THIRD-PARTY PLAINTIFF LAVENTHOL TO COUNTERCLAIMS OF THIRD-PARTY DEFENDANTS FILED MARCH 21, 1972

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. HERZFELD, Plaintiff, -against- LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, Defendant.	71 Civ. 2209 (ELP)
LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, Third-Party Plaintiff, -against- THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYER, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT and DAVID BAIRD, Third-Party Defendants.	REPLY

Defendant and Third-Party Plaintiff LAVENTHOL, KREKSTEIN, HORWATH & HORWATH ("LKH&H") by its attorneys, WILLKIE FARR & GALLAGHER, for its Reply to the Counterclaims of THIRD-PARTY DEFENDANTS ALLEN & COMPANY and ALLEN & COMPANY INCORPORATED, alleges as follows:

AS TO THE FIRST COUNTERCLAIM

1. Denies each and every allegation contained in paragraph 1 of the Counterclaim, except admits that Third-

Party Defendants ALLEN & COMPANY, INCORPORATED and ALLEN & COMPANY contend that jurisdiction is based upon Section 22(a) of the Securities Act of 1933 and Section 27 of the Securities Exchange Act of 1934 and upon the principle of pendent jurisdiction.

2. Denies each and every allegation contained in paragraph 2 of the Counterclaim, except admits that Third-Party Defendants ALLEN & COMPANY, INCORPORATED and ALLEN & COMPANY purport to bring this Counterclaim under Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934, the rules and regulations of the Securities & Exchange Commission, under Section 352-c of the General Business Law of the State of New York, and Common Law.

3. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 3 of the Counterclaim.

4. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 4 of the Counterclaim.

5. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 5 of the Counterclaim.

6. Admits the allegations contained in paragraph 6 of the Counterclaim.

7. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 7 of the Counterclaim

except denies, upon information and belief, that THE FIRESTONE GROUP, LTD. has offices located at 342 North Rodeo Drive, Beverly Hills, California.

8. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 8 of the Counterclaim.

9. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 9 of the Counterclaim.

10. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 10 of the Counterclaim.

11. Denies each and every allegation contained in paragraph 11 of the Counterclaim, except admits that it was retained by THE FIRESTONE GROUP, INC. ("FIRESTONE") to perform accounting services and further admits that it prepared and issued a report dated December 6, 1969 which expressed an opinion on the audited financial statements of FIRESTONE for the period December 26, 1968 to November 30, 1969.

12. Denies each and every allegation contained in paragraph 12 of the Counterclaim.

13. Denies each and every allegation contained in paragraph 13 of the Counterclaim, except admits that on or about December 6, 1969 LKH&H completed and issued a report of that date to FIRESTONE expressing an opinion on certain

audited financial statements of FIRESTONE attached thereto, and refers this Court to said report (a copy of which is annexed hereto) for all of the matters contained therein.

14. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 14 of the Counterclaim.

15. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 15 of the Counterclaim.

16. Denies having knowledge or information thereof sufficient to form a belief as to the truth of each and every allegation contained in paragraph 16 of the Counterclaim.

17. Denies each and every allegation contained in paragraph 17 of the Counterclaim, and refers this Court to the copy of the report which is annexed hereto for all of the statements contained therein.

18. Denies each and every allegation contained in paragraph 18 of the Counterclaim, and refers this Court to the copy of the report which is annexed hereto for all of the statements contained therein.

19. Denies each and every allegation contained in paragraph 19 of the Counterclaim.

20. Denies each and every allegation contained in paragraph 20 of the Counterclaim.

21. Denies each and every allegation contained in paragraph 21 of the Counterclaim.

22. Denies each and every allegation contained in paragraph 22 of the Counterclaim, and refers this Court to the copy of the report which is annexed hereto for all of the statements contained therein.

23. Denies each and every allegation contained in paragraph 23 of the Counterclaim.

24. Denies each and every allegation contained in paragraph 24 of the Counterclaim.

AS TO THE SECOND COUNTERCLAIM

25. In response to paragraph 25 of the Counterclaims, repeats and realleges each and every allegation, admission and denial contained in paragraphs 1 through 22 herein with the same force and effect as if set forth fully herein.

26. Denies each and every allegation contained in paragraph 26 of the Counterclaim.

27. Denies each and every allegation contained in paragraph 27 of the Counterclaim.

AS TO THE THIRD COUNTERCLAIM

28. In response to paragraph 28 of the Counterclaims, repeats and realleges each and every allegation,

admission and denial contained in paragraphs 1 through 22 herein with the same force and effect as if set forth fully herein.

29. Denies each and every allegation contained in paragraph 29 of the Counterclaim.

30. Denies each and every allegation contained in paragraph 30 of the Counterclaim.

31. Denies each and every allegation contained in paragraph 31 of the Counterclaim.

AS TO THE FOURTH COUNTERCLAIM

32. In response to paragraph 32 of the Counterclaims, repeats and realleges each and every allegation, admission and denial contained in paragraphs 1 through 22, 29 and 30 herein with the same force and effect as if set forth fully herein.

33. Denies each and every allegation contained in paragraph 33 of the Counterclaim except admits that it knew that FIRESTONE would use LKH&H's report for normal corporate purposes including the sale of certain of its securities.

34. Denies each and every allegation contained in paragraph 34 of the Counterclaim except admits that it had a duty to exercise reasonable care and diligence in issuing its December 6, 1969 Report, which duty was fully and properly discharged.

35. Denies each and every allegation contained in paragraph 35 of the Counterclaim.

36. Denies each and every allegation contained in paragraph 36 of the Counterclaim.

AS TO THE FIFTH COUNTERCLAIM

37. In response to paragraph 37 of the Counterclaims, repeats and realleges each and every allegation, admission and denial contained in paragraphs 1 through 22, 29, 30, 33, 34 and 35 herein with the same force and effect as if set forth fully herein.

38. Denies each and every allegation contained in paragraph 38 of the Counterclaim, except admits that it knew that FIRESTONE would use LKH&H's report for normal corporate purposes including the sale of certain of its securities.

39. Denies each and every allegation contained in paragraph 39 of the Counterclaim.

40. Denies each and every allegation contained in paragraph 40 of the Counterclaim.

41. Denies each and every allegation contained in paragraph 41 of the Counterclaim.

AS TO THE SIXTH COUNTERCLAIM

42. In response to paragraph 42 of the Counterclaims, repeats and realleges each and every allegation, admission and denial contained in paragraphs 1 through 22, 29, 30, 33 to 35 and 38 to 40 herein with the same force and effect as if set forth fully herein.

43. Denies each and every allegation contained in paragraph 43 of the Counterclaim.

44. Denies each and every allegation contained in paragraph 44 of the Counterclaim.

45. Denies each and every allegation contained in paragraph 45 of the Counterclaim.

FOR A FIRST AFFIRMATIVE DEFENSE TO EACH OF THE COUNTERCLAIMS, LKH&H ALLEGES:

46. The work done by defendant LKH&H in connection with the issuance of its report dated December 6, 1969 and the report itself were in conformity with generally accepted accounting principles applied on a consistent basis and defendant LKH&H had reasonable ground to believe and did believe, after performing its work in strict compliance with generally accepted auditing standards, that the statements in the said report were true and accurate.

FOR A SECOND AFFIRMATIVE DEFENSE TO EACH OF THE COUNTERCLAIMS, LKH&H ALLEGES:

47. Each counterclaim fails to state a claim upon which relief can be granted.

FOR A THIRD AFFIRMATIVE DEFENSE TO EACH OF THE COUNTERCLAIMS, LKH&H ALLEGES:

48. This Court lacks jurisdiction of the subject matter of each counterclaim asserted herein.

FOR A FOURTH AFFIRMATIVE DEFENSE TO EACH OF THE COUNTERCLAIMS, LKH&H ALLEGES:

49. ALLEN & COMPANY and ALLEN & COMPANY, INCORPORATED are estopped to assert the counterclaims asserted herein by reason of their own fraudulent conduct.

WHEREFORE, Defendant and Third-Party Plaintiff, LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, demands judgment dismissing the counterclaims of the Third-Party Defendants ALLEN & COMPANY and ALLEN & COMPANY, INCORPORATED, together with the costs and disbursements of this action.

WILLKIE FARR & GALLAGHER
Attorneys for Defendant and
Third-Party Plaintiff,
Laventhol, Krekstein, Horwath
& Horwath

By _____
(A Member of the Firm)
Office & P. O. Address
One Chase Manhattan Plaza
New York, New York 10005

LAVENTHOL KREKSTEIN HORWATH & HORWATH

CERTIFIED PUBLIC ACCOUNTANTS

3700 WILSHIRE BOULEVARD
LOS ANGELES, CALIF. 90005
(213) 381-5393

OFFICES THROUGHOUT THE WORLD

Board of Directors
The Firestone Group, Ltd.
Beverly Hills, California

We have examined the consolidated balance sheet of The Firestone Group, Ltd. and its wholly owned subsidiaries as at November 30, 1969 and the related consolidated statement of income and retained earnings from date of inception on December 26, 1968 to November 30, 1969. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, subject to the collectibility of the balance receivable on the contract of sale (see Note 4 of Notes to Financial Statements), the accompanying consolidated balance sheet and related consolidated statement of income and retained earnings present fairly the financial position of The Firestone Group, Ltd. and its wholly owned subsidiaries as at November 30, 1969 and the results of its operations from date of inception on December 26, 1968 to November 30, 1969, in conformity with generally accepted accounting principles.

Laventhol Krekstein Horwath & Horwath

Certified Public Accountants

December 6, 1969

THE FIRESTONE GROUP, LTD. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET - NOVEMBER 30, 1969

ASSETS

Current assets:		
Cash	$ 41,686	
Cash restricted (Note 2)	233,501	
Current portion of notes receivable (Note 3)	65,000	
Balance receivable on contract of sale (due in January 1970; Note 4)	4,990,250	
Deposits on purchase agreements	185,743	
Land held for sale (encumbered)	389,567	
Prepaid expenses	365,240	
Supplies inventory	20,000	
Total current assets		6,290,987
Long-term notes receivable (Note 3)	$ 6,739,607.	
Less current portion	65,000	6,674,607
Long-term portion of receivable on contract of sale (Note 4)		1,015,250
Property and equipment, at cost:		
Equipment	84,825.	
Leasehold improvements	1,047.	
	85,872.	
Less accumulated depreciation (straight-line method)	6,926.	78,946
Other assets:		
Deferred charges (Note 5)	875,418.	
Deferred income taxes (Note 6)	98,674	
Due from affiliated companies	96,073.	
Other	57,997	
Cash restricted (Note 2)	30,116.	1,158,278
		$ 15,218,068

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Notes payable, banks		$ 932,000
Contract payable (Note 4)		3,995,000
Accounts payable		624,322
Payroll taxes payable		51,324
Income taxes payable		335,437
Total current liabilities		5,938,083
Long-term notes payable (Note 3)		5,761,7
Deferred income (Notes 4 and 7)		2,834,133
Contingent liabilities and commitments (Notes * to 12)		
Shareholders' equity:		
Preferred stock, par value $1.00 per share; 2,000,000 shares authorized, none issued		
Common stock, par value $0.10 per share; 10,000,000 shares authorized, 666,666 shares issued and outstanding (Note 1)	$ 66,667	
Capital in excess of par value	550,501	
Retained earnings	66,916	684,084
		$ 15,218,068

See notes to financial statements.

FINANCIAL STATEMENTS ANNEXED TO FOREGOING REPLY

THE FIRESTONE GROUP, LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS

FROM DATE OF INCEPTION ON DECEMBER 26, 1968 TO NOVEMBER 30, 1969

Income:		
Sales		$ 22,132,607
Cost of sales		19,814,920
Gross profit on sales (before deferred gross profit)		2,317,687
Deferred gross profit (Note 4)		1,795,500
Gross profit on sales		522,187
Management fees		240,822
Interest income		218,570
Total income		981,579
Expenses:		
Operating	$ 696,801	
Interest	180,299	877,100
Income before income taxes		104,479
Income taxes:		
Current		136,237
Deferred (Note 6)		(98,674)
Net income		66,916
Retained earnings, beginning		0
Retained earnings, ending		$ 66,916
Earnings per share		0 10

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS ANNEXED TO FOREGOING REPLY
THE FIRESTONE GROUP, LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOVEMBER 30, 1969

1. The Firestone Group, Ltd. (a Delaware corporation) was incorporated on December 26, 1968. The accompanying financial statements include the accounts of the Company and all of its subsidiaries which are wholly-owned as follows:

Firestone Development Corporation
Firestone Equities Corporation
Firestone Management Corporation
Firestone Securities Corporation
Housing Resources, Inc. (see Note 8)

All material intercompany transactions have been eliminated in the accompanying financial statements.

The Company issued 499,999 shares of its common stock for cash at $1 per share. An additional 166,667 shares were issued for an assignment to The Firestone Group, Ltd. of all of the right, title and interest in three agreements to purchase parcels of real property located in the State of California. These additional shares were valued by the Board of Directors at $1 per share.

The land purchase agreements, which had no cost basis for income tax purposes, were recorded at $366,667, consisting of the value of $166,667 assigned to the common stock exchanged therefor and a liability of $200,000 for the income taxes which would be payable if the agreements were sold for this amount. The real properties underlying the three agreements were subsequently sold for $316,000.

2. An attachment of $30,116 has been filed against the Company's general funds in connection with a suit brought by a former employee. In the opinion of the Company's counsel, the suit is without merit.

Cash held in trust accounts represents interest income received in advance from syndication sales made prior to November 30, 1969. Under the terms of the syndicates' purchase agreements, these funds will become unconditionally available to the Company on January 2, 1970.

3. Long-term notes payable represent encumbrances on properties sold to syndicates on which the Company remains primarily liable. These notes bear interest of from 6.7% to 7.2% per annum. Of the long-term balance due at November 30, 1969 approximately $4,000,000 is payable in instalments through 1981 and the balance is payable in instalments through 1984.

The long-term notes receivable resulting from sales of properties to syndicates (and on which the Company remains obligated for existing first trust deeds) are collateralized by all inclusive trust deeds. These notes mature fifteen years from date of issuance. Provisions for payment require interest only for ten years and annual principal payments sufficient to amortize the notes through maturity.

6. The deferred income taxes shown under other assets represents, in the main, taxes currently payable on management fees and interest received in advance which are currently reportable for income tax purposes but which are not included as income in the consolidated income statement.

7. The syndications, to which the Company has sold property, prepay interest for a period of two years and generally prepay non-refundable management fees for a period of three years. One third of the management fees are taken into income when received. The balance of such fees together with the prepaid interest is taken into income in the periods to which they apply.

8. An employment contract with a key employee of Housing Resources, Inc. provides that he is to receive 10% of the shares of Housing Resources, Inc. Such stock, may subsequently be exchanged for common stock of The Firestone Group, Ltd. The amount of Firestone Group, Ltd. stock issuable therefor will depend upon the book value of the Housing Resources, Inc. stock and the market value of The Firestone Group, Ltd. stock at the time of exchange. At November 30, 1969, the book value of Housing Resources, Inc. capital stock was nominal.

In addition, the employee will receive an option to acquire 2,500 shares of stock in the Firestone Group, Ltd. at $10 per share.

9. Under the terms of an employment agreement, Mr. Firestone will receive a base annual salary of $60,000 plus a bonus equal to four-tenths of one percent (.004) of the Company's gross income, the bonus not to exceed an aggregate annual amount of $40,000. Mr. Scott's employment agreement provides for a base annual salary of $36,000 plus a bonus equal to twenty-four one hundredths of one percent (.0024) of the gross income of the Company, the bonus not to exceed an aggregate annual amount of $24,000. Maximum bonus has been paid for the period.

10. On January 23, 1969 the Company adopted a qualified stock option plan under which options to purchase 100,000 shares of the Company's common stock were authorized to be granted to certain employees of the Company at no less than 100% of the fair value at date of grant. As of November 30, 1969 no options had been granted under the plan. No charges will be made to income in connection with the options under the plan.

11. The Company has contracted to purchase for syndication thirteen parcels of real estate, including improved and unimproved properties at a cost of $37,449,217. These transactions are expected to close in December 1969 through April 1970.

In December 1969 the Company completed one of the acquisitions at a cost of $2,951,300. At the same time the property was syndicated for $3,043,420. In addition, the Company collected thirty-four months interest income in the amount of $384,978.

In December 1969 the Company received $100,000 in cash and subscriptions of approximately $585,000 toward a required total of $791,000 in connection with another syndication of approximately $3,155,000. The cost of the underlying property is $2,800,000.

The Company retains a profit participation of 10% upon the syndicates' reselling the properties in excess of their cost. In general, profit is defined as gross profit less all monies invested by the syndicates and 6% imputed interest thereon.

4. The Firestone Group, Ltd. acquired by contract of sale a group of convalescent hospitals containing approximately 1,900 beds. The properties were leased back to the former owners. In November, 1969 the Company sold the properties by means of a contract of sale.

The terms of the contract by which The Firestone Group, Ltd. purchased the properties provide for the following:

Assumption of existing first trust deed liens	$ 5,822,283
Note payable, secured by second trust deed, requiring monthly amortization of principal and interest at 9-1/4% for 25 years	3,540,217
Cash:	
Upon contract execution	5,000
On December 20, 1969	25,000
On January 30, 1970	3,970,000
	$ 13,362,500

The contract of sale provided for the following:

Assumption of existing trust deed liens	$ 9,362,500
Cash:	
Upon contract execution	25,000
On January 2, 1970	25,000
On January 30, 1970	4,965,250
Note secured by trust deed in favor of The Firestone Group, Ltd. requiring monthly amortization based on twenty-five years with interest of 8-1/2%; final payment due in 120th month	1,015,250
	$ 15,393,000

The sales agreement also provides for liquidated damages of $185,000 if the buyer fails to perform.

Of the total gross profit of $2,030,500, $235,000 is included in the consolidated income statement and the balance, $1,795,500 will be considered realized when the January 30, 1970 payment is received. The latter amount is included in deferred income in the consolidated balance sheet.

5. Deferred charges represent costs incurred in connection with research studies related to real estate acquisition in process and for future acquisition and educational seminars which will result in future real estate syndications. These costs are being amortized over the periods which management estimates will benefit therefrom. These periods range from 30 to 36 months.

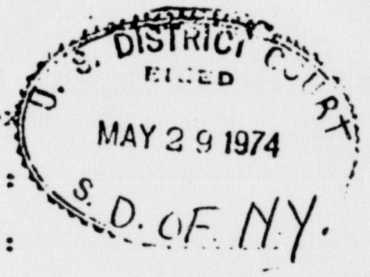
12. On November 13, 1969 the Board of Directors approved an arrangement dated November 10, 1969 with Allen & Company Incorporated for the private placement of up to $7,500,000 principal amount of 9-1/2% promissory notes of the Company due December 1, 1975 and up to 150,000 shares of the common stock of The Firestone Group, Ltd. to be sold in units of $250,000 notes and 5,000 shares of common stock at $1 per share or $255,000 per unit. The closing date for the placement is December 16, 1969. The Company will realize $7,450,000 net of fees paid in connection with the placement if the entire issue is placed.

OFFICE RECORD

7081-2

OPINION # 40,745 FILED MAY 29, 1974

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK



GERALD L. HERZFELD,

Plaintiff,

-against-

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendant.

#40745

71 Civ. 2209 (LFM)

OPINION

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Third-Party Plaintiff,

-against-

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYER, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT and DAVID BAIRD,

Third-Party Defendants.

ALLEN & COMPANY and ALLEN & COMPANY INCORPORATED,

Third-Party Counterclaimants,

-against-

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Third-Party Counterclaim Respondent.

APPEARANCES:

Blum, Haimoff, Gersen, Lipson & Szabad, New York City, for plaintiffs; Louis Haimoff, New York City, of counsel.

Willkie Farr & Gallagher, New York City, for defendant and third-party plaintiff Laventhol, Krekstein, Horwath & Horwath; Louis A. Craco, Jack David and Patricia Anne Williams, New York City, of counsel.

Pollack & Singer, New York City, for third-party defendants and third-party counterclaimants Allen & Company and Allen & Company Incorporated; Daniel A. Pollack and Martin I. Kaminsky, New York City, of counsel.

MacMAHON, District Judge.

This action was tried to the court, without a jury, on eleven trial days, commencing October 15, 1973 and ending October 29, 1973. Plaintiffs, Gerald L. Herzfeld and General Investors Co., a partnership,[1] invoking federal question and pendent jurisdiction,[2] sue the public accounting firm of Laventhol, Krekstein, Horwath & Horwath ("Laventhol") under the anti-fraud provisions of § 10(b) of the Securities Exchange Act of 1934 ("the Act"), 15 U.S.C. § 78j(b); SEC Rule 10b-5 promulgated

thereunder, 17 C.F.R. § 240.10b-5; New York General Business Law § 352-c (McKinney 1968); and the common law.

By leave of court, Laventhol has impleaded third-party defendants Irwin H. Kramer and Allen & Company Incorporated, claiming these defendants should indemnify it for any liability to plaintiffs.[3] Allen & Company and Allen & Company Incorporated (collectively "Allen") counterclaim against Laventhol seeking damages under § 10(b) of the Act, Rule 10b-5, § 352-c of the New York General Business Law, and the common law.

This action arises out of a private placement of $7.5 million of securities on December 16, 1969 by The Firestone Group, Ltd. ("FGL"), a Delaware corporation engaged in real estate syndication with its principal place of business in California. The securities in question were sold in units consisting of a $250,000 note and 5,000 shares of FGL common stock, at a price of $255,000 each. FGL hired Allen, an investment banking firm, to assist with the private placement and retained Laventhol to perform an audit of FGL's financial statements and to prepare and issue a report and audited financial statements for the eleven-month period ending

November 30, 1969. Laventhol knew that its report and audited financial statements would be relied upon by Allen and by prospective investors.

In 1971, FGL petitioned for reorganization under Chapter XI of the federal bankruptcy law. During the bankruptcy proceedings, the $250,000 notes contained in each unit were converted into 25,000 shares of FGL preferred stock, and the 5,000 shares of common stock were reverse split 10 for 1, becoming 500 shares of new common stock. The value of the units, as of October 1, 1971, was estimated at trial to be $27,750 each.

Plaintiffs and Allen contend that the report and financial statements, prepared and issued by Laventhol on December 6, 1969, were materially misleading and that their reliance on the report led to the damages they subsequently suffered.

Essentially, plaintiffs and Allen challenge the accounting treatment accorded by Laventhol to the purported purchase and sale by FGL of certain nursing home properties in November 1969. In the audited report, Laventhol treated these transactions as an acquisition and sale in which FGL first supposedly purchased the

nursing homes from Monterey Nursing Inns, Inc. ("Monterey") for $13,362,500 on November 22, 1969 and then, four days later, sold them to Continental Recreation Company, Ltd. ("Continental") for $15,393,000 on November 26, 1969. Moreover, in the report's income statement, Laventhol treated as current income $235,000 and as deferred gross profit $1,795,000 of the projected profit from the transactions.

Plaintiffs and Allen contend that the accounting treatment accorded the Monterey-Continental transactions ("Monterey transactions") was incorrect and not, as Laventhol represented, "in conformity with generally accepted accounting principles" and that the financial statements did not "present fairly the financial position" of FGL as of November 30, 1969. Specifically, they claim that the Monterey transactions were "phony" and intended solely to give support to the private placement and that Laventhol knew or should have known they were "phony," or that the transactions involved nothing more than an option to buy the property at the buyers' discretion and that Laventhol knew or should have known them to be options.

The purchase and sale of the nursing homes was the largest single transaction in the history of FGL. The magnitude and importance of the Monterey transactions can be shown by a comparison of the financial condition of FGL, with and without the Monterey transactions, as in the table below:

	Monterey Included	Monterey Excluded
Sales	$22,132,607	$6,739,607
Total Current Assets	6,290,987	1,300,737
Net Income	66,000	-169,000 (Loss)
Deferred Profit	1,795,000	None
Earnings/Share	10¢	-25¢ (Loss)

Thus, to the eye of a prospective investor, whether FGL appeared to be a profitable or unprofitable, a healthy or ailing, company depended on the recognition of the sales proceeds and the profit from the Monterey transactions in the company's financial statements. If the Monterey transactions were not included in the audited financial statements, it was likely that the private placement would not take place.

Mindful of the importance of the Monterey transactions and their treatment in the Laventhol report,

we turn to a consideration of the auditing steps taken by Laventhol with regard to these transactions.

THE AUDIT

Richard Firestone, president of FGL, called Arnold Lipkin, a Laventhol partner, in mid-November 1969 and told him that an audit of the financial statements of FGL, as of November 30, 1969, would be necessary. Laventhol then proceeded with the audit under the direction of Lipkin, as partner in charge, and Morris Schwalb, as manager of the audit. Schwalb discussed the audit with Chester Wadley, controller of FGL, on November 17, and thereafter Schwalb met with Lipkin periodically to discuss the mechanics of the audit.

A few days after November 26, when the FGL contract with Continental was reputedly signed, the existence of the FGL-Monterey and FGL-Continental contracts came to Schwalb's attention. In early December, Schwalb sought Lipkin's advice as to the proper way to report the transactions. Lipkin requested copies of the contracts and, after reading them, met with a Laventhol partner named Leonard, an expert in the hospital field, to discuss the reasonableness of the consideration in

the contracts.

Schwalb and Jerome Gottlieb, a Laventhol partner, met with Martin Scott, vice-president and director of FGL, in late November or early December. Scott informed them that Richard Firestone had initiated both agreements and that Scott was dealing with a Mr. Abramowitz, president of Monterey, in order to assemble the documentation necessary to fulfill the contract terms.

Lipkin met with Firestone on December 2 and asked him about the details of the Monterey transactions. Firestone told Lipkin that the agreements were legitimate, arms-length contracts, made in the normal course of FGL's business. Firestone also provided Lipkin with a memorandum containing references respecting Max Ruderian, president and controlling stockholder of Continental. The memorandum stated that Ruderian had been engaged in real estate syndication for fifteen years and was:

> "[T]he dean of the syndicators and has tutored almost all of the large syndication firms now operating. . . . We've know [sic] him for the last four years or so. He is very well know [sic]

> in Southern California and enjoys probably the top reputation in the field. His operations run into multi-millions of dollars annually."

The memorandum calculated Continental's net worth as "over $100,000," consisting of miniature golf courses and other assets. Ruderian's business practice was to "buy and resell prior to final payment on his sales contracts." Firestone concluded:

> "Arnold, this man and his companies are very valued contacts ..... so if you speak to him please handle him with kid gloves we don't want to lose him for future transactions."

Lipkin, an attorney and a member of the bar of Illinois (he had only practiced law for one year, in 1955), examined the Monterey contracts to determine the proper accounting treatment and concluded that they were legally enforceable. The Monterey-FGL agreement provided for payment of $5,000 on execution of the contract, $25,000 on December 20, 1969, and $3,970,000 on or before January 30, 1970. The amount of $5,822,283.09 was payable "in favor of various institutional lenders," and $3,540,216.91 was payable in equal monthly installments, at 9-1/4% interest, over twenty-five years. The

contract also stated, in Exhibit B:

> "Buyer reserves the right at any time after 1/30/70 or upon payment of the $3,970,000 cash down payment as required herein to convert this contract of sale to a conventional sale at which time Title shall pass to Buyer, subject to the existing mortgages of record and the balance of this contractual obligation shall be converted to a mortgage and note. Seller shall execute his grant deed in favor of buyer and buyer shall execute his note and mortgage in favor of seller."

The FGL-Continental contract contains identical language to that just quoted, with the substitution of the figure $4,965,250 for $3,970,000. That agreement provided for cash payments of $25,000 on execution of the agreement, $25,000 on or before January 2, 1970, and $4,965,250 on or before January 30, 1970. The amount of $9,363,500 was to be paid "in favor of various lenders," and $1,015,250 was payable in equal monthly installments, at 8-1/2% interest, over ten years. The Continental agreement also provided that:

> "Buyer shall pay to Seller in addition to those amounts already paid the sum of $185,000. in the event of failure to comply. Said additional $185,000. shall be liquidated damages."

After studying the contracts, Lipkin consulted Eli Boyer, a Laventhol partner, about Ruderian. Boyer knew Ruderian through various charitable endeavors as a man of substance and means and was familiar with Ruderian's reputation as a leading land syndicator. Boyer knew of one occasion in 1969 when Ruderian and his partner, Albert Spiegel, gave $50,000 in land and trust deeds to charity. Boyer told Lipkin all that he knew about Ruderian and early in December telephoned Ruderian, in Lipkin's presence, and spoke to him over a speaker phone about the Monterey transactions. Ruderian told Boyer that:

> "I [Boyer] should have no concern about their interest in this deal, their ability to complete it and the financial backing they had with respect to its final conclusion."

Ruderian also told Boyer that he had executed the FGL-Continental contract, regarded it as binding on Continental, and intended to comply with its terms.

After the telephone call to Ruderian, Lipkin called three bankers given as references for Ruderian in Firestone's memorandum and discussed Ruderian's

reputation and credit with them. Each replied that Ruderian was "a very legitimate, outstanding, substantial business person."

Lipkin then discussed the proper accounting treatment to be accorded the Monterey transactions with Charles Chazen, Laventhol's national partner for auditing and accounting.[5] In the course of several conversations, Chazen told Lipkin that the proper way to reflect the transactions in the financial statements was to take into current income the two $25,000 cash payments and the $185,000 in liquidated damages payable under the Continental contract. Chazen also instructed Lipkin that Laventhol could not give a "clean" or "unqualified" opinion because the down payments were too small to give the buyer more than a thin equity in the property and the buyer had no recourse against the seller because a purchase money mortgage was involved. As Chazen testified, "conservative accounting dictated a qualification with respect to the collectability of the receivable resulting from the transaction."

Due to the magnitude of the transactions, Chazen felt it wise to verify the accounting treatment

and the enforceability of the contracts with someone more experienced in real estate matters. Chazen, therefore, consulted a Laventhol partner named Zeman, who suggested that an attorney be called. With Lipkin and Zeman present, Chazen telephoned Julius Borah, a Los Angeles attorney. In a short conversation, Chazen told Borah that the contract provided for the sale of interests in land and described selected parts of the contracts to Borah, such as, the amounts involved and the fact that the agreement provided for a non-recourse note and the liquidated damage clause in the Continental contract. Chazen then asked Borah if the contract were legally enforceable, "within its terms." Borah replied that the contract was valid. Borah did not ask to see the documents, nor were the contracts read or shown to him, despite the fact that his office was only a half-hour's drive away from Laventhol's office. Chazen did not inquire of Borah whether title to the properties had passed to FGL "because I knew title hadn't passed."

Lipkin testified that the conversation with Borah confirmed his opinion that the contracts were valid and enforceable.

On December 4, Chazen and Lipkin met with Firestone, Scott and Alan Scharf, Firestone's investment advisor, at Firestone's office. The Laventhol partners told Firestone that only a portion of the $2,030,000 profit from the Monterey transactions would be reported as current income for the period ending November 30. Firestone disagreed strongly, arguing that the entire profit should be recorded as current income. Scharf agreed with Firestone and threatened Laventhol with a lawsuit if the private placement fell through. The Laventhol people remained adamant, however, and refused to alter their treatment of the profit on the Monterey transactions.

Thus, when the report was issued on December 6, the Monterey transactions were recorded as a purchase from Monterey and a sale to Continental, the profit being divided into $1,795,000 of deferred income and $235,000 of current income.

At some time during the audit, Schwalb discovered that the Monterey transactions were not recorded on the books of FGL. It was, therefore, decided that an adjusting entry was necessary and such

an entry was prepared. Schwalb instructed Wadley to make the adjusting entry on FGL's books by letter on December 19, 1969.

Laventhol also decided to issue the report as a "qualified" opinion. Thus, on December 7 or 8, Schwalb called Wadley and told him to return all copies of the report to Laventhol immediately, saying, "there will be hell to pay if we don't get them back, and don't send them by mail, send them by messenger." Wadley returned the copies of the report and Laventhol substituted a new report which stated that it fairly reflected FGL's financial condition "subject to the collectibility of the balance receivable on the contract of sale (see Note 4 of Notes to Financial Statements)." This addition was the only change in the report, and it was this "qualified" opinion which was seen by the investors, including Herzfeld.

Chazen explained the meaning of the qualification:

> "What the qualification means is that it was the auditor's concern that because of the circumstances surrounding the transaction, including the amounts

> required to be paid initially and the fact that it was a non-recourse note and the fact that it was a purchase money mortgage, that all of these considerations led the auditors to believe that they were in no position to give an opinion on the financial statements, including this receivable because of the possibility of its failure to be collected."

The qualification, however, was not intended by Laventhol to cast doubt on the transaction as a bona fide sale.

Neither the purchase from Monterey nor the sale to Continental was ever consummated. FGL never received the second $25,000 down payment or the liquidated damages, or any other additional sum of money from Continental on this transaction.

PLAINTIFFS' 10b-5 CLAIM

The essential facts which plaintiffs must prove here in order to establish a civil claim for relief under § 10(b) of the Act and Rule 10b-5 are that (1) Laventhol's report was materially misleading, (2) Laventhol knew that the report was misleading (scienter), (3) plaintiffs relied upon the report, and (4) plaintiffs suffered damages as a result of such reliance.[6]

1. WAS THE LAVENTHOL REPORT MATERIALLY MISLEADING?

We must first determine whether the audited report and financial statement issued by Laventhol was misleading in a material way. As we have discussed previously, the answer to this question turns on whether the Monterey transactions were properly reported by Laventhol.

Much has been said by the parties about generally accepted accounting principles and the proper way for an accountant to report real estate transactions. We think this misses the point. Our inquiry is properly focused not on whether Laventhol's report satisfies esoteric accounting norms, comprehensible only to the initiate, but whether the report fairly presents the true financial position of Firestone, as of November 30, 1969, to the untutored eye of an ordinary investor.

A major congressional policy underlying the anti-fraud provisions of the securities laws is the protection of investors who rely on the accuracy and completeness of information made available to them in connection with the purchase or sale of securities. Accordingly, those having greater access to information about which the investor is

presumably uninformed, or those having a special relationship to investors, have an affirmative duty of disclosure.[7] A knowing failure to discharge this obligation will justify an award of damages under Rule 10b-5.[8]

There can be no doubt that Laventhol knew that its audited report was required for the FGL private placement and that investors would be relying on the financial statements. Thus, Laventhol had a special duty to issue a truthful report, because it had access to information concerning FGL which was not available to investors and because it knew investors were depending on Laventhol, as a public accounting firm, to reveal the truth about FGL's financial condition.

Traditionally, the accounting profession and the courts have recognized that an auditor or public accountant owes a duty to the public to be independent of his client and to report fairly on the facts before him. Thus, the SEC has said: "[t]he public accountant must report fairly on the facts as he finds them whether favorable or unfavorable to his client. His duty is to safeguard the public interest, not that of his client."[9]

The full disclosure by insiders, which is mandated by the securities laws, coincides with and reinforces the accountant's professional duty to investors who read his reports. This duty cannot be fulfilled merely by following generally accepted accounting principles. Thus:

> "Compliance with generally accepted accounting principles is not necessarily sufficient for an accountant to discharge his public obligation. Fair presentation is the touchstone for determining the adequacy of disclosure in financial statements. While adherence to generally accepted accounting principles is a tool to help achieve that end, it is not necessarily a guarantee of fairness."10

Indeed, compliance with generally accepted accounting principles will not insulate an accountant from criminal culpability for fraud.[11]

> "[T]oo much attention to the question whether the financial statements formally complied with principles, practices and conventions accepted at the time should not be permitted to blind us to the basic question whether the financial statements performed the function of enlightenment, which is their only reason for existence." In re Associated Gas & Electric Co., 11 S.E.C. 975, 1058-59 (1942).

The policy underlying the securities laws of providing investors with all the facts needed to make intelligent investment decisions can only be accomplished if financial statements fully and fairly portray the actual financial condition of the company. In those cases where application of generally accepted accounting principles fulfills the duty of full and fair disclosure, the accountant need go no further. But if application of accounting principles alone will not adequately inform investors, accountants, as well as insiders, must take pains to lay bare all the facts needed by investors to interpret the financial statements accurately.

We now consider the parties' contentions in light of these guiding principles.

Plaintiffs and Allen first contend that the Monterey transactions were obviously "phony" and were concocted solely for the purpose of creating the false appearance that FGL was financially sound in order to induce investors to participate in the private placement. We think the evidence does not support the contention. Certainly, Laventhol's ascertainment of Ruderian's good reputation, coupled with his confirmation

to Laventhol of Continental's bona fides in the transaction, indicated that the sale was not "phony." We think it quite unlikely that a man of Ruderian's good business reputation would lend his name to such a scheme. Moreover, we see no reason why Continental, with assets of only $100,000, would pay $25,000 to FGL merely to create the appearance of a sale by FGL. Plaintiffs and Allen have simply failed to convince us that the Monterey transactions were "phony" much less that Laventhol knew it.

Plaintiffs claim also that the Monterey transactions were merely options and that Laventhol's failure so to characterize them was misleading. This argument rests on the language in both contracts referring to conversion of "this contract of sale to a conventional sale," the small down payments made, and a document referred to at trial as the "Amerson Memorandum" This memorandum, dated November 21, 1969, was a memorandum to Firestone, prepared by Donna Amerson, Scott's assistant, and was found in the Laventhol audit work papers.[12] It states that "[w]e have entered into an agreement for the purchase of real property on a Contract of Sale" and recites the purchase price as

$10,000,000, with down payments of $5,000, $25,000 and $2,970,000. It continued:

> "We have the option to convert the contract of sale to a conventional sale using a grant deed and trust deeds on or after 1/30/70. In the event we exercise our option to convert, the contractual obligation of approximately $2,000,000 will be converted to a second trust deed."

The memorandum also stated that the property had been sold for $11,400,000, for a profit of 14% or $1,400,000, and that "[t]he buyer shall also have the option to convert the contract of sale to a conventional sale. . . ."

Plaintiffs also direct our attention to Exhibit B of the Monterey-FGL contract, which provides that a certain computation as to the balance payable on the contract should be made "at time option is exercised."

Plaintiffs argue that these documents are convincing proof that the Monterey transactions were merely options to buy the property and that Laventhol knew it. Obviously, the Amerson memorandum[13] should have alerted Laventhol to the possibility that these contracts might

have been mere options. However, Laventhol examined the contracts themselves, which, despite the isolated appearance of the word "option" in Exhibit B to a three-page document labelled "Agreement for Sale of Real Estate," are ambiguous at best. We think the contracts, as a whole, are open to several interpretations, and the interpretation adopted by Laventhol was supportable. Boyer's conversation with Ruderian shows clearly that the president of Continental did not believe the contracts were options. Nor is there any evidence that Monterey or FGL regarded them as such. In short, plaintiffs have failed to show that the Monterey transactions were options or should have been reported by Laventhol as options.

Plaintiffs and Allen also contend that the report was misleading in a number of other material respects. The securities laws require full disclosure to investors of all material facts known to the insider. In this context, material facts are those which a reasonable investor would deem important in making his decision to buy the FGL securities.[14] Materiality, therefore, depends on whether a reasonable man in plaintiffs' position "might well have acted otherwise than to purchase" if informed of the crucial facts.[15]

We think the full and fair disclosure required by Rule 10b-5 was absent here and that, therefore, the Laventhol report was materially misleading.

First, admittedly, Laventhol itself had considerable doubt about the ability of FGL to collect the balance due on the Continental contract, or even the $4,965,250 payment due on January 30, 1970. A cursory glance at the FGL statements indicates that unless Continental made the January 30 payment FGL would be unable to make the $3,970,000 payment due to Monterey on January 30. Thus, it was incumbent on Laventhol to reveal to investors its reservations and doubts concerning consummation of the transaction and the facts upon which its reservations were based.

Laventhol claims that its qualification that the report was "subject to the collectibility of the balance receivable on the contract of sale," along with Note 4, constituted full disclosure of its reservations. We disagree.

Note 4[16] merely states the financial terms of the Monterey-FGL and FGL-Continental contracts, including the liquidated damage clause in the latter, and

recites the treatment of the profit from the transactions. We believe the note is misleading in several respects:

(1) Neither the company from whom FGL bought the properties, nor the company to whom the properties were sold, is mentioned in the note. Nor does the note mention the fact that Continental, the buyer, had a net worth of only $100,000. We think it cannot be gainsaid that a reasonable investor would regard the small net worth of Continental as an important fact in deciding whether or not to buy the FGL securities.

(2) The note says that FGL "acquired" the nursing homes. The ordinary meaning of the word "acquired" in this context, we think, can only be that FGL had acquired title to the nursing homes. This was not true. At no time did FGL ever acquire title to these properties.

(3) The note states that the deferred income of $1,795,000 "will be considered realized when the January 30, 1970 payment is received." This statement at least implies that the payment will be received on the due date. There is no suggestion of the possibility that

Continental would not carry out the contract or that the $4,965,250 payment would not be made. Considering the real doubts Laventhol had that such a payment would be made, this statement is misleading.

(4) The note states that the properties were leased back to their former owners. Laventhol had no proof that the leasing back ever occurred, except for the statement of the parties' intention to do so in the Monterey-FGL contract, and therefore this statement is misleading.

Accordingly, since we find Note 4 itself misleading, we reject Laventhol's argument that the note accurately presents Laventhol's reservations about the transactions.

Laventhol argues that the qualification as to the collectibility of the balance receivable on the sale contract "disclosed that Laventhol thought there was a possibility that the Monterey transactions might not turn out as well as all of the parties to the transactions hoped and expected they would."[17] We agree that the qualification throws some doubt on whether the transaction would be culminated, but we think more was required

of Laventhol as an independent auditor. Each investor was entitled to decide for himself, on the basis of the stark facts, whether the transaction had a realistic prospect of being completed. The information needed to make that judgment and known to Laventhol was not disclosed in the Laventhol report.

Moreover, the inclusion of the Monterey transactions in sales and income was misleading without a full disclosure by Laventhol of all the material facts about the transactions. We must remember that the investors were depending on Laventhol to tell them what was happening at FGL. And the report issued by Laventhol simply did not accurately report the financial condition of the company.

Thus, we believe that the full disclosure mandated by the Act required Laventhol to include in its report at least the following facts: (1) Continental's net worth; (2) the ambiguity of the language in the contracts which might have suggested to some that they were options;[18] (3) Ruderian, on whose reputation and representations Laventhol was depending, was not personally liable on the contracts; (4) Ruderian's practice of reselling

property before he paid for it; (5) neither of the transactions was recorded in FGL's books of original entry or corporate minute books; (6) this transaction was the largest in which FGL had ever participated; (7) FGL would show a loss if the income from the Monterey transactions were not realized; (8) FGL had not acquired title to the nursing home properties from Monterey; (9) no deed, title search or title insurance on the properties had ever been obtained by FGL; and (10) the legal opinion sought by Laventhol, on which it relied in treating the transaction as an enforceable purchase and sale, had been obtained over the telephone from an attorney who not only never saw the contract but never even had it read to him on the telephone.

We find that the Laventhol report was also misleading because it failed to disclose these facts yet reported the Monterey transaction as a sale and included the profit from the transaction in the income statement.

Moreover, the report was <u>materially</u> misleading. Thus, the facts which Laventhol failed to disclose or disclosed in a misleading way were "facts which affect the probable future of the company and . . . which may affect the desire of investors to buy, sell, or hold the company's securities."[19] We also think the facts were

material under the test of Chasins v. Smith, Barney & Co., 438 F.2d 1167 (2d Cir. 1970), in that disclosure of the true facts would have caused a reasonable man in Herzfeld's position not to buy the FGL securities.[20]

2. SCIENTER

The recent decision of the Court of Appeals, in Lanza v. Drexel & Co., 479 F.2d 1277 (2d Cir. 1973) (en banc), has dispelled any doubt in this circuit that proof of scienter is an essential element of a civil claim under 10b-5. "[N]o violation of Rule 10b-5 occurs 'in the absence of [proof] amounting to scienter, intent to defraud, reckless disregard for the truth, or knowing use of a device, scheme, or artifice to defraud. . . .'" Thus, plaintiffs must prove that Laventhol "had actual knowledge of any misrepresentations and omissions" it made, or that Laventhol's "failure to discover the misrepresentations and omissions amounted to a willful, deliberate, or reckless disregard for the truth that is the equivalent of knowledge."[21] And it has been said that "knowledge of the fact that the figures created a false picture is enough . . ." to constitute scienter.[22]

As we have shown, all the omitted facts which should have been revealed to the investors were discovered by Laventhol during the course of its audit. The evidence, thus, clearly demonstrates that Laventhol had actual knowledge of the omitted facts which render its report misleading.

Moreover, the qualification in the Laventhol report that the FGL financial statements were "subject to the collectibility of the balance receivable on the contract of sale" not only failed adequately to reveal Laventhol's admittedly grave doubts about the Monterey transactions to investors but is also indicative of the firm's knowledge that the report painted a misleading picture of the financial health of FGL. Certainly, Laventhol knew that the qualification alone, absent disclosure of the reasoning and facts which prompted it, would not alert potential investors to the uncertainties which Laventhol knew were lurking in the Monterey transactions.

Some of the Laventhol audit work papers furnish additional evidence of scienter. One document (PX 23), labelled "The Firestone Group Ltd., Notes" and dated November 30, 1969, contains the following entries:

"Estimated loss 4 months ended 4/30/69	200,000
Estimated loss 7 months ended 11/30/69	572,108
Loss before sale to Continental Recreation	772,103
Profit on sale to Continental Recreation	2,030,000
Profit before income taxes	1,257,892"

This work paper shows Laventhol's awareness of the vital importance of the Continental sale to FGL's financial health, because the transaction meant the difference between FGL's showing a profit or a loss.

Another Laventhol work paper (A-12), labelled, "Reclassification Journal Entries," and dated November 30, contains this statement:

> "Reverse entry for tax liability for sale to Continental Recreation as LKH&H will not record as a sale since not enough deposit was given Firestone."

This document shows the depth of Laventhol's doubts about the transaction and convinces us that Laventhol knew that the recording of the transaction as a sale and inclusion of the profit in the income statement was misleading, unless all the material facts were disclosed to the investors.

We find, therefore, that Laventhol had actual knowledge of the misleading nature of its report.

3. RELIANCE

Plaintiffs correctly contend that proof of reliance is not required in a case involving nondisclosure.[23] We think, however, that this case is properly characterized as one of misrepresentation, where proof of reliance is necessary. Thus, we have found that the Laventhol report misrepresented the financial condition of the company. It is of no moment that the misrepresentation in part resulted from failure to disclose material facts. We think the case no different from an accountant's false report of a company's earnings, a clear case of misrepresentation, because, in either case, the accountant makes representations which he knows are untrue. Affiliated Ute Citizens of Utah v. United States, therefore, which was grounded on a mere nondisclosure unaccompanied by any representation whatever, is inapposite.

Whether we characterize the issue as one of "reliance" or "causation," plaintiffs must show a nexus between the misrepresentations in the Laventhol report and the damage they have sustained. Thus, they must prove that "'the misrepresentation is a substantial factor in determining the course of conduct which results

in [their] loss.'"[24]

Herzfeld first heard of the FGL private placement in November 1969 from his friend, David Baird, who was a business broker. Baird told Herzfeld that Charles Allen regarded the deal as a good one and thought FGL was a very profitable company. In addition, Baird said, Allen thought that, with the 7.5 million dollars to be raised in the private placement, the company's future earnings should be even better. Herzfeld was enthusiastic about the securities after talking with Baird, especially since Charles Allen regarded the investment as a good one. Herzfeld was also encouraged by the prospect that the 5,000 shares of FGL stock in each unit would be split two for one and that FGL would buy back 5,000 shares of stock from each unit, at $25.00 per share.

Herzfeld also discussed the FGL placement in mid-November 1969 with Irwin Kramer, Charles Allen's son-in-law and a partner in Allen. Kramer told him that Charles Allen thought the deal was "the hottest deal he had ever seen" and offered to sell Herzfeld one unit.

Later in the month, Herzfeld received the FGL "Note and Stock Purchase Agreement," covering one unit of securities. He read the entire document, paying particular attention to the income statement. The income statement indicated to him that FGL was a "very profitable company," with earnings of approximately $2.00 per share. Herzfeld calculated the value of FGL stock to be $20.00 per share. The purchase agreement was accompanied by a letter from FGL advising that audited financial statements were being prepared. After reading the agreement, Herzfeld signed it, and he and his brothers also signed an agreement with David Baird, authorizing Baird, as their agent, to purchase one unit of FGL securities.

On December 16, 1969, Herzfeld received the audited Laventhol report, accompanied by a letter from FGL "explaining" the changes in the financial statements. The letter also advised Herzfeld that:

> "If for any reason you find that the changes reflected in the audited financial statements are of a nature which would have resulted in a change of your investment decision, we will arrange to promptly refund to you your subscription payment against receipt of our Note and Stock."25

Herzfeld read the letter and the income statement in the Laventhol report, which was the only part of the report he read. He paid particular attention to the earnings indicated and was very impressed by the deferred gross profit of $1,795,000. The latter figure, he understood, meant "that this is a profit that the company had made and was going to pick up in a subsequent accounting period."

The evidence clearly shows that the Laventhol report was a substantial factor in Herzfeld's decision to buy the securities and his subsequent loss. It is true that his initial interest in the securities was generated by sources other than Laventhol and that he actually purchased both units before seeing the audited report. Nevertheless, FGL's offer to refund the buyer's subscription payment left open the possibility that Herzfeld would rescind the agreement if the report had indicated that the securities were not a good investment. The income statement, however, only reinforced Herzfeld's belief that FGL was a profitable company. A true statement of the financial condition of the company, we believe, would have shaken that belief and possibly caused Herzfeld to change his mind and demand a refund of his

payment. The report's false picture of FGL's financial condition was, thus, a substantial, even crucial, factor in convincing Herzfeld that his investment decision to purchase the securities was right. We find, therefore, that plaintiffs have shown sufficient reliance on the Laventhol report.[26]

4. DAMAGES

Herzfeld and General Investors Co. purchased two units of FGL securities for $510,000 and recouped $357,000 when they settled their claims against Allen and the other original defendants. They seek to recover the $153,000 difference, plus 9-1/2% interest on $510,000, for the period September 1, 1970[27] until November 11, 1971,[28] and interest of 9-1/2% on $153,000 for the period from November 11, 1971 to the date of trial. Laventhol admits that plaintiffs are entitled to their out-of-pocket loss of $153,000, if it is liable, but objects to both awards of interest as contrary to the proper measure of damages under the Act.

We think that both parties have overstated plaintiffs' out-of-pocket loss. There was evidence at trial that each unit of FGL securities is now worth

$27,750. Thus, plaintiffs' two units are worth $55,500, and their out-of-pocket damage is only $97,500.

The Herzfelds' interest claims amount, essentially, to the interest they expected to receive on the notes from FGL. Thus, the interest was part of the profit they expected to make from their investment.

The Act prohibits a damaged party from recovering "a total amount in excess of his actual damages on account of the act complained of."[29] Actual damage does not include loss of anticipated profits. Recovery is limited to plaintiffs' out-of-pocket loss.[30] Since plaintiffs' interest claims are really claims for lost profits, they may not recover them under 10b-5, and they are entitled only to actual damages of $97,500.[31]

THE HERZFELDS' CLAIM UNDER THE NEW YORK GENERAL BUSINESS LAW

Plaintiffs also claim that Laventhol violated § 352-c of the New York General Business Law. Laventhol contends that § 352-c is a penal statute and does not authorize a private right of action based on its violation and that, in any event, it has not violated the statute. We reject the contention.

The statute makes it a misdemeanor to engage in fraud or misrepresentation "where engaged in to induce or promote the issuance, distribution, exchange, sale, negotiation or purchase. . . of any securities . . . ."[32] The purpose of the statute is to protect the public against fraud in the sale of securities.[33]

In Barnes v. Peat, Marwick, Mitchell & Co., 69 Misc.2d 1068 (Spec. Term 1972), the court denied a motion to dismiss a cause of action under § 352-c because a private right of action could be inferred from the statute. 69 Misc.2d 1072. On appeal, the Appellate Division affirmed Special Term's decision on the motion to dismiss. 42 App.Div.2d 15 (1st Dep't 1973).[34] We think, considering the recent decision of the Appellate Division in Barnes, the cited federal cases, the purpose of the statute, and the policy of the New York courts to imply a civil cause of action from a criminal statute designed to protect the public,[35] that we must find that § 352-c authorizes a private right of action by a person injured by its violation.

The elements of a private cause of action under § 352-c are uncertain, since it appears no

reported New York case has gone to trial. It is claimed, however, that neither reliance nor scienter need be shown to establish a violation of § 352-c. We think, nevertheless, that proof of reliance in the sense of causation must be shown, for otherwise a defendant could be held liable under § 352-c even to purchasers whose damage could not be traced to his wrongdoing.

As we have shown in our discussion on the claim under 10b-5, plaintiffs have demonstrated the requisite reliance or causation here. As to scienter, the statute makes it unlawful to make "[a]ny representation or statement which is false, where the person who made such representation or statement . . . knew the truth. . . ."[36] The evidence shows that the Laventhol report, taken as a whole, falsely portrays the financial condition of FGL and that Laventhol knew the truth. We find, therefore, that Laventhol violated § 352-c and is liable to plaintiffs for their out-of-pocket damage, $97,500, caused by that violation.

Plaintiffs' claims for the specified 9-1/2% interest must be denied. Damages for fraud under New York law are limited to the actual pecuniary loss sustained by plaintiff,

and all elements of profit are excluded. Since the private right of action under § 352-c is essentially a fraud action,[37] the common law fraud damage rule is applicable.[38]

PLAINTIFFS' COMMON LAW CLAIMS

Plaintiffs make a variety of claims under the common law, including claims for (1) breach of contract as third-party beneficiaries, (2) negligence, and (3) common law fraud or deceit.

1. THE CONTRACT CLAIM

The complaint alleges that plaintiffs are third-party beneficiaries of the contract under which FGL retained Laventhol to audit FGL's financial statements as of November 30, 1969, and that Laventhol breached that contract by negligently preparing its report. No evidence directed to such a claim was presented at trial. Nor do plaintiffs even argue this claim in their brief. Nonetheless, we must deal with it.

A third-party beneficiary must prove that the contract clearly expresses an intention to benefit him before he can enforce the contract in his favor.[39] It

is not enough that a third party is an incidential beneficiary of a contract. The parties must intend that the contract operate to benefit the third-party beneficiary.[40]

The evidence here is that any benefit accruing to plaintiffs from Laventhol's audit was incidental. FGL commissioned Laventhol to perform the audit solely because Allen refused to close the private placement without an audit. There is no evidence that the parties intended to benefit plaintiffs, and, therefore, they may not recover as third-party beneficiaries of the FGL-Laventhol contract.

2. FRAUD AND NEGLIGENCE

Plaintiffs also seek to recover damages from Laventhol under theories of common law negligence and fraud. The law of New York as to an accountant's liability to third parties for negligent conduct is unclear.[41] Moreover, we think this case is better viewed as one involving fraud or deceit than negligence, and that plaintiffs are entitled to recover under the rule of Ultramares Corp. v. Touche, 255 N.Y. 170 (1931).

In Ultramares, while refusing to find that the defendant accountant was liable for negligent conduct, the Court of Appeals (Cardozo, Chief Judge), said:

> "The defendants owed to their employer a duty imposed by law to make their certificate without fraud, and a duty growing out of contract to make it with the care and caution proper to their calling. . . . To creditors and investors to whom the employer exhibited the certificate, the defendants owed a like duty to make it without fraud, since there was notice in the circumstances of its making that the employer did not intend to keep it to himself." 255 N.Y. at 179.

Here, Laventhol had a duty to investors, including plaintiffs, not to act fraudulently, since the circumstances of the audit indicated that FGL would be showing the report to other persons. Indeed, Laventhol knew the report was being made exclusively for the private placement. Thus, Laventhol is liable to plaintiffs for any fraud in its report.

To recover for fraud, plaintiffs must prove that (1) Laventhol made a false representation of a material fact, (2) Laventhol knew it was false, (3) Laventhol made the representation with intent to deceive

investors and to induce them to rely upon it, (4) plaintiffs did rely upon it, and (5) plaintiffs suffered damage as a result.[42] We have already found that Laventhol's report contained material misrepresentations. We must still determine whether plaintiffs have proved sufficient scienter ((2) and (3)) and reliance ((4)) to recover for fraud.

Although we have found that Laventhol knew its report contained misrepresentations, plaintiffs must still establish that the misrepresentations were made with an intent to deceive them and other investors. As we have seen, Laventhol knew that its report was misleading and knew that it would be delivered to and relied upon by investors. Given these facts, surely Laventhol believed that its report would mislead or convey a false impression and thus deceive investors. The requisite scienter was, therefore, shown. Ultramares Corp. v. Touche, supra, 255 N.Y. 187.[43]

Plaintiffs must also show that they justifiably relied upon the report and that reliance led to damage. The misrepresentation must have played a material and substantial part in leading plaintiffs to

adopt their course of action.[44] The fraudulent misrepresentation need not, however, be the sole inducing cause for a plaintiff's conduct.[45] It is sufficient that the representation was a material inducing cause.[46]

The evidence at trial clearly established that Herzfeld's actions were at least partially induced by the Laventhol report. Thus, he relied upon it to reinforce his belief that FGL was a profitable company. Herzfeld's decision to buy the securities was undoubtedly affected by several other factors, especially his conversations with Baird and Kramer, but the Laventhol report convinced him, at a time when he could have rescinded the purchase, that the FGL securities were a wise investment. Thus, it cannot be said that the Laventhol report was not a material inducing cause of Herzfeld's and his brothers' purchase of the securities.

Finally, plaintiffs must show that they suffered damage as a result of the fraud. Plaintiffs were, as the evidence shows, damaged in the amount of $97,500 as a result of their purchase of the FGL securities. Since recovery for fraud in New York is limited to plaintiff's actual pecuniary loss,[47] plaintiffs' damages are

limited to their out-of-pocket injury and their interest claims must be denied.

Plaintiffs having satisfied the elements of a cause of action for deceit or common law fraud, we find Laventhol is liable to plaintiffs under the common law for $97,500.

THIRD-PARTY CLAIM

Laventhol, in its third-party complaint, seeks indemnity or contribution from Allen and Irving H. Kramer for damages it owes to plaintiffs as a result of our decision in favor of the plaintiffs in the main action.

In support of its claim over, Laventhol contends that Allen and its officer Kramer "touted" the FGL units by exaggerating their true value. The only conduct by either Allen or Kramer arguably approaching "touting" occurred when, during a social dinner, Kramer told Herzfeld that although he had no first-hand knowledge of the offering, Charles Allen felt that it was one of the hottest deals he had ever seen. Before this dinner conversation occurred, however, and unbeknownst to Kramer, David Baird had so thoroughly convinced Herzfeld that

the offering was all but irresistible that Herzfeld not only agreed to advance money for Baird's purchase of one unit, in return for 75% of any profits, but also agreed to assume the entire risk of loss from the investment. We think, under the circumstances, that Kramer's "touting," if any, neither heightened Herzfeld's eagnerness nor affected his decision to purchase an additional unit. Therefore, the third-party complaint must be dismissed as against Kramer.

Laventhol also contends that Allen misstated to investors the true import of the Laventhol report by knowingly obscuring "the fact that the Laventhol audited report did not confirm the unaudited statements which had been previously circulated to the investors." It is undisputed that the unaudited financial report, which had been distributed to investors on or about November 10, 1969, projected FGL income as $315,000 for the eleven-month period ended November 30, 1969, whereas the Laventhol audited report of December 6, 1969 showed FGL net income to be only $66,916 for virtually the same period. [48]

Laventhol's charge of misconduct by Allen is levelled at the dual role of Lee Meyer in the transaction.

Meyer, one of three directors of FGL and a vice president of Allen, supervised the private placement for Allen. Although Meyer did not participate in the preparation of the unaudited financial statements, he admitted reading them and discussing them with Firestone, and he paid special attention to the "bottom line" or net income figure of $315,000. Meyer also received, read and discussed the audited Laventhol report and expressed dissatisfaction with the significantly lower net income figure reported there. Thus, there can be no doubt that Allen, through its officer Meyer, was aware of the major discrepancies between the net income figures in the audited and unaudited financial statements.

There is also evidence to the effect that Allen, through Meyer, participated in discussions leading to the preparation of a letter, dated December 16, 1969, which both minimized and obscured the differences between the audited and unaudited financial statements.

Feinberg, Allen's attorney at the time the letter was prepared, testified that Meyer was present on December 15, 1969, when Feinberg and others began to prepare a summary of discrepancies between the audited and

unaudited financial statements. The following day, December 16, a list of discrepancies appeared in a letter sent to investors. We can conceive of no reason for discussing discrepancies and preparing such a list on December 15 other than to incorporate the list into the December 16 letter.

The letter, after describing the discrepancies between the conflicting financial statements, stated that "none of these changes have resulted or will result in an adverse change in the financial condition or the results of our operations." Obviously, the letter was intended to still investors' doubts about the private placement and convince them that the differences between the unaudited and audited financial statements were of no consequence.

Since the net income figure in the unaudited statementswas nearly five times greater than the net income figure in the Laventhol audited report, the statement in the letter, if not blatantly false, was plainly misleading. Thus, we find that Allen, through Meyer, knowingly misled investors by minimizing the material discrepancies between the audited and unaudited statements.

Finally, Laventhol claims that Meyer, motivated by a $200,000 profit for Allen, unsuccessfully pressured Laventhol to accede to Firestone's demand that its report show a substantially greater net profit by including all the unrealized profit from the Monterey transaction in the current accounting period.

Meyer, in his role as one of three directors of FGL, was thoroughly familiar with FGL's operations, and, although he testified that he was not active in the day-to-day management of the company, he did attend board meetings, review financial statements and observe operations. There can be no question that he was familiar with the Monterey transaction and its importance in FGL's total financial picture. We think the facts support the inference that he knew whether the units were a sound investment.

There is conflicting testimony as to whether Meyer attempted to influence Laventhol's accounting treatment of the Monterey transaction. Chazen and Lipkin, on the one hand, are certain that they spoke with Meyer and others during a speaker telephone conference on December 11, 1969, and Chazen relies on his time sheet to

confirm the conversation. Both recall that Meyer was adamant in his demand that all the income anticipated from the Monterey transaction be reported as current income. Feinberg, on the other hand, said that he was present in New York on December 15, 1969, when a speaker telephone conference was held among Meyer, Firestone, Scott, Scharff and himself in New York and Lipkin and another Laventhol partner in California. He testified that Meyer did not tell Laventhol how to treat the Monterey transaction but merely questioned the propriety of Laventhol's treatment of the anticipated income.

Feinberg did testify, however, that because of the discrepancies between the unaudited and audited financial statements, "I thought we had a real problem in completing the placement" and that Meyer appeared to be "very, very upset and shaken . . . by the results . . . shown in the financial statements."

Meyer also testified that he in no way attempted to influence Laventhol. He first said that he questioned Lipkin about the financial statement on December 15, 1969, when Lipkin personally delivered it to New York. After Meyer left the stand, Lipkin testified that his time sheet

showed that he had not been in New York on December 15, 1969. Moreover, he was positive that he had not been in New York on that date because he had not been there for thirty-five years, except to attend a hearing before the Attorney General of New York some time subsequent to December 15, 1969. Confronted with Lipkin's testimony and the time sheet, Meyer changed his story. He conceded that his only conversation with Lipkin was by telephone and explained that he was confused in his earlier testimony about meeting him in New York on December 15.

Richard Firestone testified that Meyer agreed with his position that all the anticipated income from the Monterey transaction should be shown in the current accounting period, but he was unsure whether Meyer ever tried to convince Laventhol to change its report in accordance with his position.

We find Meyer's demeanor, his monetary motive to color the offering, his agreement with Firestone's position on the report, his participation in the preparation of the minimizing letter, and his changed story about meeting with Lipkin in New York on December 15, 1969 cast considerable doubt on the reliability of his

testimony and the accuracy of his recollection.

In light of Meyer's inside knowledge of FGL's operation and, particularly, the Monterey transaction, we conclude that he had knowledge of the misleading nature of the report yet failed to disclose material facts to correct its misleading character. Allen is chargeable with knowing participation with Laventhol in misrepresentation and fraudulent nondisclosure of material facts. As underwriter of the private placement, Allen, no less than Laventhol, had a duty to reveal all the material facts needed by investors to enable them to make an intelligent investment decision. Allen plainly failed to fulfill its duty of full and fair disclosure to investors. Worse, had Meyer succeeded in his efforts to inflate the reported income in the audited report, the report would have become even more misleading than it was.

Even though we have resolved the material factual issues raised by the third-party claim in favor of Laventhol, we still must deny Laventhol a right to indemnity from Allen. The most [illegible] has been shown is that Allen was guilty of knowing participation in Laventhol's and Firestone's fraudulent misconduct, either

as an aider and abettor,[49] a joint tortfeasor,[50] a co-conspirator, or other joint wrongdoer.[51] One who intentionally joins in the perpetration of a fraud is denied a right of indemnity from others participating in the wrong, whether the claim is predicated on violation of the securities laws or the common law.[52] The full disclosure policy of the securities laws would be thwarted if an accountant could avoid paying damages to a defrauded plaintiff simply by shifting the ultimate burden of loss for his wrongdoing to a jointly culpable underwriter through indemnity.

Laventhol's claim for contribution, however, rests on firmer ground. Contribution among joint wrongdoers is appropriate in a § 10(b) or Rule 10b-5 action.[53] The district court in Globus, quoting de Haas, held that:

> "'[T]hose sections of the [securities acts] which expressly provide for civil liability contain express provisions for contribution among intentional wrongdoers. . . . Since the specific liability provisions of the Act provide for contribution, it appears that contribution should be permitted when liability is implied under Section 10(b).'"[54]

The policy underlying the securities laws is not frustrated by permitting contribution. Rather, that policy is reinforced. Contribution, unlike indemnity, does not permit a wrongdoer to escape loss by shifting his entire responsibility for damages to another party. Instead, it apportions the loss among the joint wrongdoers so that the deterrent effect of the judgment will be felt by all culpable parties. To deny contribution would be to dilute the deterrent effect of the securities laws, since Allen, a participant in Laventhol's fraud, would escape responsibility for its wrongdoing.

In a similar case, State Mut. Life Assur. Co. of America v. Peat, Marwick, Mitchell & Co., 49 F.R.D. 202 (S.D.N.Y. 1969), the court, relying on N.Y. CPLR § 1401 (McKinney 1963), denied contribution to a joint wrongdoer on procedural grounds, holding that contribution is not permitted "unless a joint judgment has been recovered against the joint tortfeasors and the one seeking contribution has paid more than his pro-rata share of the judgment."[55] We feel, however, that in these days of mounting litigation costs, not to mention ever-greater demands on judicial time, such insistence

on circuitous procedural mechanisms is unwarranted and unnecessary. Rather, the underlying goals of the securities laws, fairness to the parties, and judicial economies dictate that all disputes arising out of the same transaction should be settled in one proceeding. This can easily be accomplished by bringing the third party into the prime action under Fed.R.Civ.P. 14 or, for that matter, CPLR § 1007.[56]

Under Dole v. Dow Chem. Co., 30 N.Y.2d 143 (1972), Laventhol may, as it has, implead Allen and seek to recover a portion of the damages it must pay to plaintiffs. "No joint judgment is required and if one of the tortfeasors is sued, he has the right to implead the other and charge the latter. . ." with his share of the judgment.[57] It follows, therefore, that Laventhol is entitled to recover contribution from Allen. We must now decide what portion of plaintiffs' damages are to be borne by Allen.

There are two alternatives available for calculating the amount of Allen's contribution to Laventhol. Laventhol's liability to plaintiffs can be shared pro rata with Allen, or allocated relative to the degree of

fault of Allen and Laventhol. We feel that in a securities fraud case, such as this, the pro rata method is more appropriate.

> "'The only workable rule to apply . . . is the one of pro rata contribution. . . . On the whole, judged by administrative expediency, this is probably as simple and satisfactory a way to handle the matter as any. To resort to fault, compensation, or extent of participation would be even more confusing.'"58

Furthermore, if we were to apportion the liability of Laventhol and Allen on the basis of their participation in the fraud, we would reach the same result. Although Laventhol prepared and disseminated the misleading report, it was encouraged to do so by Allen, which was equally aware of its misleading nature. In fact, Allen unsuccessfully sought to have Laventhol make changes in the report, the effect of which would have been to render it even more misleading. There can be no doubt that Allen and Laventhol were equally culpable. They will thus be held equally responsible. Laventhol is entitled to pro rata contribution from Allen in the amount of one-half of $97,500.

COUNTERCLAIM

Allen counterclaims against Laventhol claiming violations of § 10(b) of the Act, Rule 10b-5, § 352-c of the New York General Business Law, and the common law. Significantly, Allen does not counterclaim for indemnity or contribution. Rather, although Allen admittedly purchased no units at the initial offering on December 16, 1969, it now purports to stand in the shoes of original innocent purchasers of the units as assignee of their claims against Laventhol. Allegedly, the assignments were made when the purchasers settled their claims against Allen. Allen claims to be subrogated to its assignors' rights and, therefore, seeks to "recover from Laventhol any and all damages they [the assignors] sustained regardless of what Allen paid them."[59] Thus, although Allen paid each assignor only $100,000 for each $255,000 unit, it seeks to recover damages of $227,250 per unit, a clear profit to Allen of $127,250 per unit.[60]

Laventhol contends that Allen is precluded from recovering on its counterclaim because Allen stands in pari delicto with Laventhol. If Allen were permitted to recover on its assigned claims, Laventhol argues,

underwriters would be encouraged to engage in wrongdoing similar to that practiced here by Allen. Laventhol's argument requires us to review the state of the law concerning the in pari delicto defense in securities fraud cases.

The term "in pari delicto" means "in equal fault,"[61] and the defense is usually allowed where "the plaintiff has knowingly participated as an equal in the illegal act which caused the loss."[62]

Allen and Laventhol, as we noted earlier, were equally culpable in issuing the misleading audited report. Each knew that the report falsely depicted FGL's financial condition but made no attempt to reveal that fact to investors. Allen, moreover, not only attempted to make the report more misleading, but participated in minimizing the discrepancies between the audited and unaudited reports. Allen and Laventhol are, therefore, in pari delicto.

Few courts have considered whether the in pari delicto defense should be allowed in a securities case where the parties are equal participants in a fraud. Three courts, however, have denied recovery to a plaintiff

whose wrongdoing constituted active fraud.[63]

In Moscarelli v. Stamm, the court denied plaintiff's motion for partial summary judgment, noting that while plaintiff's mere participation in the violation did not bar his recovery per se, instigation or wilful participation by plaintiff in the violation might bar recovery.[64]

Similarly, in Serzysko v. Chase Manhattan Bank, the court found that plaintiff's recovery for violation of Regulation U was precluded because he had knowingly and intentionally procured or induced that violation by intentionally making false statements to the defendant.[65] The court reasoned that allowing plaintiff to recover "would be to encourage rather than discourage deception on the part of investor-borrowers with resulting prejudice to the observance of the margin requirements of the Act."[66]

In Kuehnert v. Texstar Corp., plaintiff, a tippee, sued an insider for violation of § 10(b) claiming that defendant had revealed false inside information to him, on which he traded and was damaged. The Court of Appeals for the Fifth Circuit held that the district

court had properly refused to allow plaintiff, as a tippee, to assert defendant's violation of § 10(b), because to permit recovery would encourage tippees to trade on the inside information they acquire. The court noted, however, that application of the in pari delicto defense rested with the discretion of the court and that "[t]he question must be one of policy: which decision will have the better consequences in promoting the objective of the securities laws by increasing the protection to be afforded the investing public."[67]

Although our Court of Appeals has not considered the appropriateness of in pari delicto in a § 10(b) case, it has questioned the applicability of the defense in a suit for violation of the margin regulations.[68] However, the court expressly refused to "follow" or "attack" the holdings of Serzysko or Moscarelli because "the kinds of contributory fault there involved go beyond knowledge of the margin requirements to concealment or misstatement of material facts."[69] Thus, Pearlstein v. Scudder & German leaves us free, as was the court in SEC v. Packer, Wilbur & Co., 362 F. Supp. 510, 514-15 (S.D.N.Y. 1973), to apply the in pari delicto defense to cases involving "a wilful misstatement of material facts" by a

claimant.[70]

We think the discretionary, policy-oriented approach adopted by the Fifth Circuit in Kuehnert is appropriate here and that the protection of investors envisaged by the securities laws can better be promoted by denying Allen recovery.

If the defense of in pari delicto is ever appropriate in a securities case, and we think it is, this is such a case. Allen was not a passive investor who merely borrowed money from a bank, or a broker, knowing that the margin regulations were thereby violated. Rather, Allen was an active participant in Laventhol's issuance of a misleading report and sought not only to profit from Laventhol's fraud but to compound it by providing investors with even less information than Laventhol. It would be absurd and unconscionable to allow Allen to reap a huge profit by asserting the fraud claims of innocent investors when the fraud would never have occurred had Allen acted in accordance with its duty as an underwriter.

More importantly, however, allowing Allen recovery here would encourage, rather than discourage, fraud

by underwriters involved in securities transactions because they could then profit from their fraud by settling with the victims for less than the value of their claims and assert those claims against other participants in the fraud. The better result, we think, is to deny Allen recovery on its assigned claims, thus ensuring that future underwriters will think twice before entering into a fraudulent scheme. Such a result also provides the maximum deterrence against violation of the securities laws.

Therefore, since Allen is barred from asserting its assignors' claims, the counterclaim must be dismissed.

The foregoing opinion constitutes this court's findings of fact and conclusions of law, in accordance with Rule 52(a), Fed.R.Civ.P.

Accordingly, the Clerk of the court is directed to enter judgment:

(1) in favor of plaintiffs against defendant Laventhol for damages in the amount of $97,500, with costs;

(2) in favor of third-party plaintiff Laventhol against third-party defendant Allen for damages in the amount of $48,750, with costs;

(3) in favor of third-party defendant Irving H. Kramer against third-party plaintiff Laventhol dismissing the third-party complaint as against Irving H. Kramer; and

(4) in favor of third-party plaintiff Laventhol against third-party defendant Allen dismissing Allen's counterclaim.

So ordered.

Dated: New York, N. Y.
May 29
[redacted], 1974

LLOYD F. MacMAHON
United States District Judge

Herzfeld v. Laventhol, Krekstein, Horwath & Horwath

71 Civ. 2209-LFM

FOOTNOTES

1

By leave of court, General Investors Co. was added as a party plaintiff during trial. Originally, this action was brought against various parties, including Allen. On November 11, 1971, plaintiff settled his claims with all defendants, except Laventhol. An amended complaint was then filed, naming Laventhol as sole defendant.

2

15 U.S.C. § 78aa.

3

The third-party complaint names as third-party defendants Firestone Group, Ltd., Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyer, Irwin H. Kramer, Richard Firestone, Martin Scott and David Baird. Firestone Group, Ltd., Firestone and Meyer were never served. Laventhol voluntarily discontinued the third-party action against all defendants, except Irwin Kramer and Allen & Company, Incorporated.

4

Lipkin did not testify to the substance of this conversation.

5

Chazen testified that the national partner for accounting and auditing "is responsible for developing the firm's auditing standards, interpreting accounting principles as they are pronounced by the various bodies, acting in an advisory capacity, providing authoritative source for information which may be required during the course engagements, developing the firm's accounting and auditing manuals, and generally being the last word in accounting and auditing."

6

SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969).

7

Chris-Craft Indus., Inc. v. Piper Aircraft Corp., 480 F.2d 341, 363 (2d Cir.), cert. denied, 414 U.S. 910 (1973).

8

See SEC v. Texas Gulf Sulphur Co., supra, 401 F.2d at 854-55.

9

Touche, Niven, Bailey & Smart, 37 S.E.C. 629, 670 (1957). See also, Rule 1.01, Code of Professional Ethics of the American Institute of Certified Public Accountants (1969); Drake v. Thor Power Tool Co., 282 F. Supp. 94, 104 (N.D. Ill. 1967); T. Sonde, The Responsibility of Professionals under the Federal Securities Laws--Some Observations, 68 Nw. U.L.Rev. 1, 3 (1973); Securities--Rule 10b-5--Accountant Held to Duty to Disclose Material Errors in Certified Financial Report Discovered Subsequent to Filing, 43 N.Y.U. L.Rev. 209, 211, 216 (1968).

10

T. Sonde, supra, 68 Nw. U.L.Rev. at 4.

11

United States v. Simon, 425 F.2d 796, 806-07 (2d Cir. 1969), cert. denied, 397 U.S. 1006 (1970).

12

This memorandum was admitted solely as a document brought to the attention of Laventhol. We do not consider it, therefore, as evidence of the truth of its contents. C.T. McCormick, Law of Evidence § 228 at 464-65 (1954).

13

We may not, and do not, consider the memorandum for proof of its contents.

14

SEC v. Texas Gulf Sulphur Co., supra, 401 F.2d at 849; List v. Fashion Park, Inc., 340 F.2d 457, 462 (2d Cir.), cert. denied, 382 U.S. 811 (1965); Chris-Craft Indus., Inc. v. Piper Aircraft Corp., supra, 480 F.2d at 362-63.

15

Chasins v. Smith, Barney & Co., 438 F.2d 1167, 1171 (2d Cir. 1970).

16

Because of its importance, we reproduce Note 4 here in its entirety:

"4. The Firestone Group, Ltd. acquired by contract of sale a group of convalescent hospitals containing approximately 1,900 beds. The properties were leased back to the former owners. In November, 1969 the Company sold the properties by means of a contract of sale.

The terms of the contract by which The Firestone Group, Ltd. purcha properties provide for the following:

Assumption of existing first trust deed liens	$ 5,822,283
Note payable, secured by second trust deed, requiring monthly amortization of principal and interest at 9-1/4% for 25 years	3,540,217
Cash:	
Upon contract execution	5,000
On December 20, 1969	25,000
On January 30, 1970	3,970,000
	$ 13,362,500

The contract of sale provided for the following:

Assumption of existing trust deed liens	$ 9,362,500
Cash:	
Upon contract execution	25,000
On January 2, 1970	25,000
On January 30, 1970	4,965,250
Note secured by trust deed in favor of The Firestone Group, Ltd. requiring monthly amortization based on twenty-five years with interest of 8-1/2%; final payment due in 120th month	1,015,250
	$ 15,393,000

The sales agreement also provides for liquidated damages of $185,000 if the buyer fails to perform.

Of the total gross profit of $2,030,500, $235,000 is included in the consolidated income statement and the balance, $1,795,500 will be considered realized when the January 30, 1970 payment is received. The latter amount is included in deferred income in the consolidated balance sheet."

17

Laventhol post-trial brief at 24-25.

18

While we declined to find that the contracts were options, a reasonable investor might have considered the ambiguity of the language in the contracts important.

19

SEC v. Texas Gulf Sulphur Co., supra, 401 F.2d at 849. "In each case then, whether facts are material within Rule 10b-5 when the facts relate to a particular event and are undisclosed by those persons who are knowledgeable thereof will depend at any given time upon a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity." Id. "The materiality test is concerned only with whether a prototype reasonable investor would have relied [citation omitted]. Account must be taken of all the surrounding circumstances to determine whether the fact under consideration is of such significance that a reasonable investor would weigh it in his decision whether or not to invest." Chris-Craft Indus., Inc. v. Piper Aircraft Corp., supra, 480 F.2d at 363.

20

Chasins v. Smith, Barney & Co., supra, 438 F.2d at 1171.

21

Lanza v. Drexel & Co., 479 F.2d 1277, 1304-06 (2d Cir. 1973) (en banc); Cohen v. Franchard Corp., 478 F.2d 115, 123 (2d Cir.), cert. denied, 414 U.S. 857 (1973); Shemtob v. Shearson, Hammill & Co., 448 F.2d 442, 445 (2d Cir. 1971).

This is not the rule in several other circuits, where scienter is not a necessary element of a 10b-5 claim. See, Ellis v. Carter, 291 F.2d 270, 274 (9th Cir. 1961); Royal Air Properties, Inc. v. Smith, 312 F.2d 210, 212 (9th Cir. 1962); Stevens v. Vowell, 343 F.2d 374, 379-80 (10th Cir. 1965); Myzel v. Fields, 386 F.2d 718, 734-35 (8th Cir. 1967), cert. denied, 390 U.S. 951 (1968); City Nat'l Bank v. Vanderboom, 422 F.2d 221, 229-30 (8th Cir.), cert. denied, 399 U.S. 905 (1970).

22

Republic Technology Fund, Inc. v. Lionel Corp., 483 F.2d 540, 551 (2d Cir. 1973).

23

Affiliated Ute Citizens of Utah v. United States, 406 U.S. 123, 153-54, reh. denied, 407 U.S. 916, 408 U.S. 931 (1972). See also Mills v. Electric Auto-Lite Co., 396 U.S. 375, 385 (1970); Cohen v. Franchard Corp., supra, 478 F.2d at 124; Chris-Craft Indus., Inc. v. Piper Aircraft Corp., supra, 480 F.2d at 374-75.

24

List v. Fashion Park, Inc., supra, 340 F.2d at 462; Globus v. Law Research Serv., Inc., 418 F.2d 1276 (2d Cir. 1969), cert. denied, 397 U.S. 913 (1970); Siegel v. Realty Equities Corp. of N.Y., 54 F.R.D. 420, 424-25 (S.D.N.Y. 1972); Wertel v. Kramarsky, 61 F.R.D. 674, 681 (S.D.N.Y. 1974).

25

Plaintiffs' Exhibit 6.

26

Laventhol contends that plaintiffs cannot be found to have relied on the report because they did not read Note 4 or any other part of the report, except the income statement. However, we have found that part of the report on which plaintiffs did rely misleading, and, as we previously found, neither Note 4 nor any other part of the report would have presented plaintiffs with a true picture of the company's financial state.

27

The date on which FGL ceased paying interest on the notes.

28

The date of Herzfeld's settlement with Allen and the other defendants.

29

15 U.S.C. § 78bb(a).

30

Janigan v. Taylor, 344 F.2d 781, 786 (1st Cir.), cert. denied, 382 U.S. 879 (1965); Estate Counseling Serv., Inc. v. Merrill Lynch, Pierce, Fenner & Smith, 303 F.2d 527, 533 (10th Cir. 1962); Schaefer v. First Nat'l Bank of Lincolnwood, 326 F. Supp. 1186, 1193 (N.D. Ill. 1970), appeal dismissed, 465 F.2d 234 (7th Cir. 1972). A defrauded seller, however, might be able to recover the profits made by an insider in violation of 10b-5. Janigan v. Taylor, supra.

31

Our holding as to plaintiffs' interest claims does not bar their recovery of prejudgment interest on damages, an issue we do not now decide.

32

N.Y. General Business Law § 352-c-1(c) (McKinney 1968).

33

Herdegen v. Paine, Webber, Jackson & Curtis, 31 Misc.2d 104 (Sup. Ct. 1961).

34

We disagree totally with Laventhol's contention that the Appellate Division's decision left "in question the authority of the denial of the motion to dismiss" by the Special Term. The Appellate Division did modify the order of the Special Term to stay the action pending disposition of several related class actions in federal court, but this modification had no effect whatsoever on the disposition of the motion to dismiss, which was affirmed. 42 App.Div.2d at 15-16. Federal courts which have considered this issue have come to a similar conclusion. Lupardo v. I.N.M. Indus. Corp., 36 F.R.D. 438 (S.D.N.Y. 1965); American Bank & Trust Co. v. Barad Shaff Sec. Corp., 335 F. Supp. 1276, 1283 (S.D.N.Y. 1972). Cf. Briskin v. Glickman, 276 F. Supp. 600 (S.D.N.Y. 1967).

35

Atkin v. Hill, Darlington & Grimm, 15 App.Div.2d 362 (1st Dep't 1962), aff'd, 12 N.Y.2d 940 (1963).

36

N.Y. General Business Law § 352-c-1(c).

37

Herdegen v. Paine, Webber, Jackson & Curtis, supra.

38

Reno v. Bull, 226 N.Y. 546, reargument denied, 227 N.Y. 591 (1919); Hanlon v. MacFadden Publications, Inc., 302 N.Y. 302 (1951); 3 N.Y. Jr., Fraud and Deceit § 254 at 336-37.

39

Cerullo v. Aetna Cas. & Sur. Co., 41 App.Div.2d 1, 4 (4th dep't 1973).

40

Associated Flour Haulers & Warehousemen, Inc. v. Hoffman, 282 N.Y. 173 (1940); H.R. Moch Co. v. Rensselaer Water Co., 247 N.Y. 160 (1923); Hylte Bruks Aktiebolag v. Babcock & Wilcox Co., 399 F.2d 289, 292 (2d Cir. 1968); 10 N.Y. Jur., Contracts §§ 239, 240 at 160-62.

41

See, Ultramares Corp. v. Touche, 255 N.Y. 170 (1931); State St. Trust Co. v. Ernst, 278 N.Y. 104 (1938); Euro-Continental, Inc. v. Cogen, 131 N.Y.S.2d 20 (Sup. Ct., Spec. Term 1954), aff'd, 137 N.Y.S.2d 829 (1st Dep't 1955); Rusch Factors, Inc. v. Levin, 284 F. Supp. 85 (D.R.I. 1968).

42

Jo Ann Homes at Bellmore, Inc. v. Dworetz, 25 N.Y.2d 112, 119 (1969); Channel Master Corp. v. Aluminum Ltd. Sales, Inc., 4 N.Y.2d 403, 407 (1958); Sabo v. Delman, 3 N.Y.2d 155, 159 (1957); Prosser, Law of Torts § 100 at 700 (3d ed. 1964); 24 N.Y. Jur., Fraud and Deceit § 14 at 47-48.

43

Prosser, supra, § 102 at 715.

44

Prosser, supra, § 108 at 714.

45

Dress Shirt Sales, Inc. v. Hotel Martinique Associates, 12 N.Y.2d 339, 343 (1963).

46

State St. Trust Co. v. Ernst, supra, 278 N.Y. at 122.

47

Reno v. Bull, supra.

48

The Laventhol audited report includes income and retained earnings for a period five days longer than the eleven-month period shown in the unaudited financial statement.

49

Chris-Craft Indus., Inc. v. Piper Aircraft Corp., supra, 480 F.2d at 370.

50

Melodee Lane Lingerie Co. v. American Dist. Tel. Co., 18 N.Y.2d 57 (1966); Darby v. Prewitt, 12 N.Y.2d 100 (1962).

51

See generally, Prosser, supra, § 44.

52

Globus v. Law Research Serv., Inc., supra, 418 F.2d at 1287-89; de Haas v. Empire Petroleum Co., 286 F. Supp. 809 (D. Col. 1968); Kuehnert v. Texstar Corp., 412 F.2d 700 (5th Cir. 1969); 3 L. Loss, Securities Regulation 1831 (1961).

53

Globus, Inc. v. Law Research Serv., Inc. 318 F. Supp. 955 (S.D.N.Y. 1970), aff'd on opinion below, 442 F.2d 1346 (2d Cir. 1971); de Haas v. Empire Petroleum Co., supra. See also 3 L. Loss, supra, at 1739-1740 n.178.

54

Globus, Inc. v. Law Research Serv., Inc., supra, 318 F. Supp. at 958.

55

49 F.R.D. at 212.

56

See Dole v. Dow Chem. Co., 30 N.Y.2d 143, 149 (1972).

57

J.M. McLaughlin, Supplementary Practice Commentary to N.Y. CPLR § 1401 (McKinney 1972).

58

3 L. Loss, supra, at 1738, quoting with approval Douglas and Bates, The Federal Securities Act of 1933, 43 Yale L.J. 171, 178-181 (1933); Globus, Inc. v. Law Research Serv., Inc., supra, 318 F. Supp. at 958. See also Kuehnert v. Texstar Corp., supra, 412 F.2d at 705 n.7.

59

Allen brief, at 108.

60

Allen bought seven complete units of FGL securities and part of an eighth unit, consisting of 7,739 shares of FGL convertible preferred stock and 150 shares of FGL common stock; Allen paid its assignor $30,600 for the fraction of a unit.

61

Black's Law Dictionary 893 (4th ed. 1957); Perma Life Mufflers, Inc. v. International Parts Corp., 392 U.S. 134, 135 (1968).

62

Comment, 54 Minn. L.Rev. 878, 879 (1970).

63

Kuehnert v. Texstar Corp., 286 F. Supp. 340 (S.D. Tex. 1968), aff'd, 412 F.2d 700, supra; Serzysko v. Chase Manhattan Bank, 290 F. Supp. 74 (S.D.N.Y. 1968), aff'd per curiam, 409 F.2d 1360 (2d Cir.), cert. denied, 396 U.S. 904 (1969); Moscarelli v. Stamm, 288 F. Supp. 453 (S.D.N.Y. 1968).

64

288 F. Supp. at 459-460.

65

290 F. Supp. at 87.

66

Id. at 89-90.

67

412 F.2d at 704. Courts in this district have split on whether in pari delicto will bar recovery by a tippee under § 10(b). See Nathanson v. Weis, Voisin, Cannon, Inc., 325 F. Supp. 50 (S.D.N.Y. 1971); Wohl v. Blair & Co., 50 F.R.D. 88 (S.D.N.Y. 1970).

68

Pearlstein v. Scudder & German, 429 F.2d 1136 (2d Cir. 1970). As the Court of Appeals noted in Pearlstein, congress placed the responsibility for observing the margin regulations on the broker, by forbidding him to extend undue credit, but did not forbid customers from accepting such credit. 429 F.2d at 1141. Thus, in pari delicto may be an inappropriate defense for a broker who has violated the margin regulations. Section 10(b), however, forbids the conduct practiced by both Allen and Laventhol here, and, therefore, the rationale adopted by the court in Pearlstein is not applicable to this case.

69

429 F.2d at 1142. We note, as did Judge Friendly in his dissent in Pearlstein, 429 F.2d at 1148, that Serzysko was affirmed by the Second Circuit "in all respects." 409 F.2d 1360. Moreover, we do not regard Perma Life Mufflers, Inc. v. International Parts Corp., supra, to be pertinent since in that antitrust case plaintiff was coerced into participating in the defendant's violation of the statute. The court did not decide whether "truly complete involvement and participation in a monopolistic scheme could ever be a basis, wholly apart from the idea of in pari delicto, for barring a plaintiff's cause of action." 392 U.S. at 140.

70

362 F. Supp. at 514. See also Avery v. Merrill Lynch, Pierce, Fenner & Smith, 328 F. Supp. 677, 680 (D.D.C. 1971); Aubin v. H. Hentz & Co., 303 F. Supp. 1119, 1121 (S.D. Fla. 1969).

United States District Court
FOR THE
Southern District of New York

GERALD L. HERZFELD,

Plaintiff,

-against-

LAVENTHOL, KREKSTEIN,
HORWATH & HORWATH,

Defendant.

OPINION

LLOYD F. MacMAHON, D. J.

71 Civ. 2209-LFM

OFFICE RECORD

Received
Served
Filed 5-29-74
5-30-74

AFFIDAVIT OF DEFENDANT/THIRD PARTY PLAINTIFF LAVENTHOL IN OPPOSITION TO MOTION TO AMEND JUDGMENT OF THIRD-PARTY DEFENDANTS FILED JUNE 14, 1974

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. HERZFELD, Plaintiff, -against- LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, Defendant.	
LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, Third-Party Plaintiff, -against- ALLEN & COMPANY INCORPORATED and IRWIN H. KRAMER, Third-Party Defendants.	71 Civ. 2209 (LFM) AFFIDAVIT IN OPPOSITION TO A MOTION OF THIRD-PARTY DEFENDANTS TO AMEND CERTAIN FINDINGS AND TO AMEND THE JUDGMENT
ALLEN & COMPANY and ALLEN & COMPANY INCORPORATED, Third-Party Counterclaimants, -against- LAVENTHOL, KREKSTEIN, HORWATH & HORWATH, Third-Party Counterclaim Respondent.	

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

LOUIS A. CRACO, being duly sworn, deposes and says:

1. I am a member of the Bar of this Court and a member of the firm of Willkie Farr & Gallagher, attorneys for Laventhol Krekstein Horwath & Horwath ("Laventhol"). I submit this affidavit in opposition to the motion of Allen & Company and Allen & Company Incorporated ("Allen") to amend certain findings and conclusions in the Opinion of this Court dated May 29, 1974 and to amend the judgment.

2. Allen moves this Court to effectively retract the conclusion that Allen is liable in Laventhol's third-party action to contribute one-half the amount of the judgment against Laventhol. Allen contends that the Court should give Allen credit for its participation with others in a 1971 settlement with Herzfeld and change the third-party action judgment that Allen must pay Laventhol half the amount of the judgment against Laventhol. Allen's motion should be denied because the Opinion already takes the 1971 settlement into account, contains ample findings for the conclusion that Allen is responsible for any such liability as may be imposed on Laventhol, is not rendered inaccurate with respect to Allen's culpability by any new evidence and because the 1971 settlement is not relevant to Allen's liability in the present action by Herzfeld or the third-party action because they are separate and distinct from the 1971 settlement.

3. The Opinion's recognition of the 1971 settlement cannot be gainsaid. The very first note of the seventy notes to the Opinion states in part that "on November 11, 1971, plaintiff settled his claims with all defendants, except Laventhol." The amount Herzfeld received in settlement, $357,000, is noted on page 36 of the Opinion.

Thus, in concluding that Allen is liable for one-half of any judgment against Laventhol, the Court fully considered the 1971 settlement in which Allen was a participant.

4. The Opinion is replete with findings to sustain the view that Allen was responsible for Laventhol's being cast in damages:

> "Thus, there can be no doubt that Allen, through its officer Meyer, was aware of the major discrepancies between the net income figures in the audited and unaudited financial statements." (Opinion p. 47)
>
> * * *
>
> "There is also evidence to the effect that Allen, through Meyer, participated in discussions leading to the preparation of a letter, dated December 16, 1969, which both minimized and obscured the differences between the audited and unaudited financial statements." (Opinion p. 47)
>
> * * *
>
> "Since the net income figure in the unaudited statements was nearly five times greater than the net income figure in the Laventhol audited report, the statement in the letter, if not blatantly false, was plainly misleading. Thus, we find that Allen, through Meyer, knowingly misled investors by minimizing the material discrepancies between the audited and unaudited statements." (Opinion p. 48)

5. Allen's motion to be relieved of its obligation to contribute to the judgment against Laventhol is not based on any facts of which the Court was unaware in rendering its Opinion. Allen offers no new evidence which would warrant disturbing the Opinion's findings and conclusions respecting Allen's culpability.

6. The 1971 settlement which Allen urges as a basis for excusing it from the obligation to contribute to the payment of the judgment against Laventhol is of no relevance to Laventhol's third-party claim for contribution from Allen. Allen's counsel all but concedes this at page 120 of the Transcript.

7. In the 1971 settlement, Herzfeld received $357,000 (as noted in the Court's Opinion at p. 36) and in return, released eleven parties from his claims against them for $510,000. The eleven parties were Allen, Charles Allen, Irwin Kramer, The Firestone Group, Ltd., Lee Meyer, Richard Firestone, Martin Scott, Holtzmann, Wise & Shephard, James Deer, and Jacobs, Persinger & Parker. Thereafter, Herzfeld served an Amended Complaint asserting claims against Laventhol alone and seeking $200,000 in damages. Laventhol's Third-Party Complaint against Allen sought indemnification and contribution for Allen's wrongdoing to the extent of any liability which Laventhol might have as a result of the claims asserted in the Amended Complaint.

8. It would be unfair for the Court to endorse Allen's argument that Allen should be relieved of its obligation to pay half the judgment against Laventhol because Allen participated in the 1971 settlement between Herzfeld and eleven other persons but Laventhol did not. In fact, the reason Laventhol did not participate was that Allen excluded Laventhol even though it knew that Laventhol would have claims against Allen for contribution and indemnification if Herzfeld proceeded with an action against Laventhol. Shortly after Laventhol learned of the 1971 settlement, counsel for Allen told counsel for Laventhol that Allen had specifically

instructed him to conduct the settlement negotiations in secret so as to exclude Laventhol from the settlement. The reason given to counsel for Laventhol was that Allen was angry with Laventhol.

9. When Laventhol learned of the proposed 1971 settlement, Laventhol strongly protested against its exclusion from the negotiations and from the settlement. Laventhol also opposed the settlement because it had cross-claims for contribution and indemnity against other defendants, and especially against Allen. Nevertheless, Judge Palmieri approved the settlement. However, Judge Palmieri explicitly stated that upon Herzfeld's service of an Amended Complaint, Laventhol could serve a third-party complaint alleging its claims against Allen and others.

10. It is incontrovertible that the $357,000 paid to Herzfeld in 1971 was paid to induce Herzfeld to release all of the persons against whom he had asserted claims except Laventhol. Had Allen not excluded Laventhol from the settlement, Herzfeld would not have served an Amended Complaint, Laventhol would not have had to serve its Third-Party Complaint, and a trial of this action would not have been necessary.

11. Should Allen now be permitted to prevail and to escape its liability to Laventhol, it will have established through the back door a bar to claims for contribution from non-settling parties. This result is clearly undesirable and stands contrary to the policy of the Federal Securities Laws.

WHEREFORE, it is respectfully requested that the Motion of Third-Party Defendant Allen be denied in all respects.

Louis A. Craco

Louis A. Craco

Sworn to before me this

14th day of June, 1974.

Jacob L. Todres

Notary Public

JACOB L. TODRES
NOTARY PUBLIC, State of New York
No. 24-4514051
Qualified in Kings County
Commission Expires March 30, 1975

JUDGMENT AND ORDER #74,498
FILED JUNE 13, 1974

U.S. DISTRICT COURT
FILED
JUN 13 1974
S. D. OF N.Y.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

GERALD L. KARZFELD

Plaintiff

-against-

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH

Defendant

JUDGMENT
#74,498

71 Civil 2209 (LFM)

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH

Third-Party Plaintiff

-against-

THE FIRESTONE GROUP, LTD.
ALLEN & COMPANY, INCORPORATED
ALLEN & COMPANY, CHARLES ALLEN,
LEE W. MAGEE, IRWIN H. KRAMER,
RICHARD H. FIRESTONE, MARTIN A.
SCOTT and DAVID BAIRD

Third-Party Defendants

ALLEN & COMPANY and ALLEN &
COMPANY INCORPORATED

Third-Party Counterclaimants,

-against-

LAVENTHOL, KREKSTEIN, HORWATH & HORWATY

Third-Party Counterclaim Respondent.

The above entitled action having been settled as to all defendants, except Laventhol, on November 11, 1971. An amended complaint was then filed, naming Laventhol as sole defendant. Laventhol voluntarily discontinued the third-party action against all defendants, except Irwin Kramer and Allen & Company, Incorporated.

The action having been brought on for trial before the Honorable Lloyd F. MacMahon, United States District Judge, on October 16, 17, 19, 23, 25, 26 and 29, 1973, and at the conclusion of the evidence the Court having reserved decision, and the Court thereafter on May 29, 1974, having handed down its opinion, containing its findings of fact and conclusions of law pursuant

Herzfeld -v- Laventhol,et al- 71 Civil 2209 (LFM)

Judgment cont'd

to Rule 52(a), of the Federal Rules of Civil Procedure, and directing the Clerk to enter judgment, it is,

ORDERED, ADJUDGED and DECREED: That plaintiff GERALD L. HERZFELD have judgment against defendant LAVENTHAL, KREINSTEIN, HORWATH & HORWATH in the amount of $97,500., with costs; it is further,

ORDERED, ADJUDGED and DECREED: That the third-party plaintiff LAVENTHOL, KREINSTEIN, HORWATH & HORWATH, have judgment against third-party defendant ALLEN & COMPANY, INCORPORATED for damages in the amount of $40,750., with costs; it is further,

ORDERED, ADJUDGED and DECREED: That third-party defendant IRVING H. KRAMER have judgment against third-party plaintiff LAVENTHOL, KREINSTEIN, HORWATH & HORWATH, dismissing the third-party complaint; and it is further,

ORDERED: That the counterclaim of ALLEN & COMPANY INCORPORATED against LAVENTHOL, KREINSTEIN, HORWATH & HORWATH, be and it is hereby dismissed.

Dated: New York, N.Y.
June 13, 1974

Raymond F. Burghardt
CLERK

At a Slated Term of the United States District Court for the Southern District of New York, held in the United States Court House in the Borough of Manhattan, City of New York on the day of in the year of our Lord, One Thousand Nine Hundred and Seventy

PRESENT:
HONORABLE: LLOYD F. MAC MAHON
United States District Judge.

GERALD L. HERZFELD

vs.

LAVENTHOL KREKSTEIN HORWATH & HORWATH, et al

Docket No. 71Civil 2209

Now comes the Plaintiff By BLUM HAIMOFF GERSEN LIPSON & SZABAD, by Louis Haimoff.

and moves the trial of this cause. Likewise comes the Defendant by WILLKIE FARR& GALLAGHER, by Louis A. Craco and Jack David, 3rd pty defts POLLACK & SINGER, by Daniel A. Polls

Non Jury

Thereupon a Jury is duly empaneled and sworn, and the cause proceeds to Trial. 10-16-73

and adj. till 10-18-73 at 12 Noon

10-19-73 Trial Continued

10-22-73 " "

10-25-73 " "

10-26-73 " "

10-29-73 " "

10-30-73 Trial Concluded

Adj. Decision Reserved

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

----------X

GERALD L. HERZFELD,

Plaintiff,

- against -

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Defendant.

----------X

INDEX NO.
71 Civ. 2209

PRE-TRIAL ORDER

LAVENTHOL, KREKSTEIN, HORWATH & HORWATH,

Third-Party Plaintiff,

- against -

THE FIRESTONE GROUP, LTD., ALLEN & COMPANY, INCORPORATED, ALLEN & COMPANY, CHARLES ALLEN, LEE W. MEYERS, IRWIN H. KRAMER, RICHARD M. FIRESTONE, MARTIN A. SCOTT and DAVID BAIRD,

Third-Party Defendants.

----------X

I. Stipulation As To Facts And Documents

1. On or prior to December 16, 1969, The Firestone Group, Ltd. ("Firestone"), sold to approximately 24 investors $7,500,000 of 9 1/2% Promissory Notes and 150,000 shares of Common Stock. Said securities were sold in Units, each Unit consisting of a Note, in principal amount of $250,000, and 5,000 shares of the stock at $1 per share, the purchase price for each Unit being $255,000.

2. Jacobs, Persinger & Parker, 70 Pine Street, New York, New York ("Jacobs"), counsel for Firestone, in a letter

dated December 16, 1969, listed Gerald L. Herzfeld, of "General Investor Company, 295 Fifth Avenue, 4th Floor, New York, N.Y." and David Baird, of "Baird, Patrick & Co., 67 Broad Street, New York, N.Y. 10004", as persons to each of whom one Unit of the Firestone securities had been issued (Plaintiff's Exh. 31).

3. In a letter dated November____, 1969, David G. Baird and Messrs. Nathan E. Herzfeld, Saul S. Herzfeld, and Gerald L. Herzfeld agreed that Baird would purchase a Unit of the Firestone securities in his own name, but as agent for the Herzfelds as principals; under the agreement, the Herzfelds were required to furnish Baird with the sum of $255,000 by certified or official bank checks payable to Firestone (Plaintiff's Exh. 1).

4. Plaintiff delivered to Holtzman, Wise & Shepard at 30 Broad Street, New York, New York, cashier's checks of Century National Bank & Trust Company and Chase Manhattan Bank, each dated December 15, 1969, and each in the amount of $255,000, payable to Firestone (Plaintiff's Exhs. 5A, 5B). The funds utilized in purchasing the said cashier's checks were furnished in equal parts by Nathan E. Herzfeld, Gerald L. Herzfeld, and Saul S. Herzfeld (Plaintiff's Exhs. 26, 27, 28A, 29A, 29B, 30).

5. The Note and Stock Purchase Agreement, dated November 10, 1969, executed by Gerald L. Herzfeld (Plaintiff's Exh. 3) included, as Exhibit B, an unaudited projected statement of income of Firestone for the 11 months ended November 30, 1969.

6. On November 12, 1969, Firestone mailed a letter

to David Baird of Baird, Patrick & Co., 67 Broad Street, New York, New York 10004, enclosing four copies of a Note and Stock Purchase Agreement dated November 10, 1969, and a similar letter with like enclosures, dated November 21, 1969, was mailed by Firestone to Gerald L. Herzfeld of General Investor Company, 295 Fifth Avenue, Fourth Floor, New York, New York (Plaintiff's Exhs. 32, 2). By these letters, the closing of the sale and purchase was set for Tuesday, December 16, 1969, at the offices of Holtzman, Wise & Shepard, 30 Broad Street, New York, New York, special counsel for the purchasers; and Firestone undertook to deliver to the purchasers, at the closing, audited financial statements of Firestone as, at and for the eleven months ended November 30, 1969.

7. A letter, dated December 16, 1969, was delivered by Holtzman, Wise & Shepard, 30 Broad Street, New York, New York, "To Each of the Purchasers of Units of The Firestone Group, Ltd. Pursuant to Purchase Agreements, dated November 10, 1969", including plaintiff and Baird, and enclosed various documents referred to therein, including a copy of a certificate of the President of Firestone, and a letter dated December 16, 1969 from Firestone, referred to in the certificate of the President (Plaintiff's Exh. 8).

8. The certificate dated December 16, 1969, purporting to bear the signature of Richard L. Firestone as President, refers to a letter of even date from Firestone to each purchaser accompanying the transmittal of Firestone's audited financial statement as, of and for the eleven month period ended November 30, 1969 (Plaintiff's Exh. 33).

9. The letter dated December 16, 1969, delivered to plaintiff and Baird, refers to the prior undertaking by Firestone to deliver copies of its audited financial statements for the period December 26, 1968 to November 30, 1969, and encloses "for your information, copies of these financial statements certified by Laventhol, Krekstein, Horwath & Horwath, certified public accountant" (Plaintiff's Exh. 6). This letter puported to grant to plaintiff the right to rescind the purchase upon the basis of any changes reflected in the audited financial statements, said right of rescission to be exercised on or before January 9, 1970.

10. Firestone retained defendant Laventhol, Krekstein, Horwath & Horwath ("Laventhol") to perform accounting services and pursuant to said retainer, Laventhol prepared and issued a report dated December 6, 1969.

11. On or within a few days after December 16, 1969 (prior to January 9, 1970), plaintiff received a report, dated December 6, 1969, purporting to have been prepared and issued by Laventhol (Plaintiff's Exh. 7).

12. The Report to Stockholders of Firestone for the nine months ending January 31, 1970, includes a statement by Richard M. Firestone, as President, as follows (Plaintiff's Exh. 9):

> "You may recall too that we entered into a contract of sale for a large property of convalescent hospitals. The transaction involved initial payments prior to closing which was scheduled for

January 30, 1970. After making these payments, the buyer requested an extension to July 1. We obtained an even longer extension from the seller and granted the buyer the requested time...with the understanding that we have the right to sell it to a third party. As a backstop, we have been proceeding to do just that and expect to be able to obtain at least the same price elsewhere."

13. On March 30, 1971, an Involuntary Petition in Bankruptcy was filed against Firestone in the United States District Court, Central District of California, and on April 1, 1971, Firestone filed a Chapter XI Petition. On October 1, 1971, an order confirming an arrangement was filed. On or about August 18, 1971, Gerald L. Herzfeld filed a proof of claim in the Chapter XI proceeding, in the amount of $500,000, with interest at 9 1/2% per annum from September 1, 1970. Annexed to the proof of claim were copies of Notes of Firestone to the order of David Baird in the amount of $250,000 and to the order of Gerald L. Herzfeld, in the amount of $250,000. Under the plan of arrangement, plaintiff received a payment of $51,000 in respect of the $500,000 claim filed (Plaintiff's Exhs. 34, 35,36).

14. When this action was originally commenced on or about May 18, 1971, the defendants were: The Firestone Group, Ltd., Allen & Company, Incorporated, Allen & Company, Charles Allen, Lee W. Meyers, Irwin H. Kramer, Richard M. Firestone, Martin A. Scott, Holtzmann, Wise & Shepard, James W. Deer, Jacobs, Persinger & Parker, and Laventhol, Krekstein, Horwath & Horwath. On or about November 3, 1971, plaintiff's claim against the foregoing defendants, other than Laventhol, was settled and the action

discontinued against said defendants, other than Laventhol. On or about November 3, 1971, Gerald L. Herzfeld, Nathan E. Herzfeld, Saul S. Herzfeld, and General Investors Co. executed releases to each of the said defendants, other than Laventhol. In each of said releases, the signatory thereto purported to reserve his or its rights against Laventhol (Plaintiff's Exh. 10).

15. Plaintiff's Exhibits 11 through 25 are papers which were contained in defendant's files kept in connection with the accounting services which it performed for Firestone, and were produced by the defendant during discovery in this action.

II. Stipulation As To Facts In The Third-Party Action

1. Plaintiff Gerald L. Herzfeld asserts no claim of any kind in this action against any party other than defendant Laventhol.

2. Charles Allen never made any representations of any kind to Laventhol in connection with Firestone.

3. Irwin Kramer never made any representations of any kind to Laventhol in connection with Firestone.

4. Allen & Co. never made any representations of any kind to Laventhol in connection with Firestone.

5. Irwin Kramer was a vice-president of Allen & Co. Inc. in November and December, 1969.

6. Lee Meyers was a vice-president of Allen & Co. Inc. in November and December, 1969.

7. Arnold Lipkin was the partner of Laventhol in charge of the audit of Firestone in November and December, 1969.

8. Morris Schwalb was the manager for Laventhol of the audit of Firestone in November and December, 1969.

9. At the closing of the private placement of December 16, 1969, Allen & Co. Inc. was furnished with an audited financial statement and report of Firestone for the period ending November 30, 1969 prepared by Laventhol and dated December 6, 1969.

III. Issues To Be Tried

The issues to be tried, as between plaintiff and defendant Laventhol, are set forth in the trial briefs heretofore filed with the Court.

IV. Exhibits To Be Offered By Defendants In The Third-Party Action

Third-party defendant Allen & Co. Inc. intends to offer in evidence the following documents, reserving its right to offer such additional documents as may be indicated by the testimony at trial:

A-1 Contract, Firestone and Monterey Nursing Inns Inc., 11/22/69 (previously plaintiff's Exhibit 12).

A-2 Contract, Firestone and Continental Recreation Co. Ltd. ("Continental"), 11/26/69 (previously plaintiff's Exhibit 13).

A-3 Memo, R. M. Firestone to A. Lipkin, 12/2/69 (previously plaintiff's Exhibit 14).

A-4 Laventhol Financial Statement for Firestone dated 12/6/69 for period ending 11/30/69 (previously third-party defendants' Exhibit 21) -- withdrawn.

A-5 Laventhol Financial Statement for Firestone dated 12/6/69 for period ending 11/30/69 (previously third-party defendants' Exhibit 20).

A-6 Memo, Ruderian of Continental to Firestone 1/30/70 (previously thir-party defendants' Exhibit 24).

A-7 Draft of Laventhol Financial Statement for Firestone for period ending 1/30/69 (previously third-party defendants' Exhibit 16).

A-8 Laventhol Financial Statement for Firestone (previously third-party defendants' Exhibit 17).

A-9 "Consolidated Worksheet" of Laventhol for Firestone (3 pages) (previously third-party defendants' Exhibit 18).

A-10 12 pages of worksheets of Laventhol for Firestone (previously third-party defendants' Exhibit 27).

A-11 "Additional Adjusting Entries" of Laventhol for Firestone (2 pages) (previously plaintiff's Exhibit 10).

A-12 "Reclassification Journal Entries" of Laventhol for Firestone dated 12/16/69 (previously third-party defendants' Exhibit 22).

A-13 "Other Deferments" of Laventhol for Firestone dated 12/6/69 (previously third-party defendants' Exhibit 30).

A-14 Letter from M.A. Schwalb of Laventhol to C. Wadley of Firestone, 12/18/69.

A-15 Letter from Firestone to Allen & Company, as agent, 12/16/69.

Dated: New York, New York
October 16, 1973

SO ORDERED:

S/ WILKIE, FARR

S/ BLUM, HAMOFF

S/ POLLACK & SINGER

J.D.C.

TRIAL TRANSCRIPT DATED OCTOBER 15, 1973

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

GERALD L. DEUTZFELD, Plaintiff, vs THE FIRESTONE GROUP, LTD. et al., Defendants.	71 Civil 2209

New York, N. Y.

October 15, 1973 - 2:30 p.m.

Before

HON. LLOYD F. MacMAHON,

District Judge

APPEARANCES:

BLUM, KAMIOFF, GERSEN, EPSON & SZADAD, Esqs.,
Attorneys for Plaintiff
LOUIS KAMIOFF, Esq., of Counsel

WILKIE, FARR & GALLAGHER, Esqs.,
Attorneys for Lowenthal, Krekstein, Horwath & Horwath
LOUIS A. CRACO, Esq., and
JACK DAVID, Esq., of Counsel

POLLACK & SPIGER, Esqs.,
Attorneys for Allen & C., Inc., Allen & Co.,
Charles Allen and Irwin H. Kramer
DANIEL L. POLLACK, Esq.,
MARTIN I. KRAMSKY, Esq., and
PAUL E. LEWIS, Esq., of Counsel

THE COURT: Good afternoon.

THE CLERK: Gerald L. Herzfeld versus The Firestone Group, Ltd. et al.

MR. HAIMOFF: Plaintiff is ready.

MR. CRACO: Defendant is ready.

MR. POLLACK: Third-party defendant is ready.

THE COURT: Proceed.

MR. HAIMOFF: Would your Honor care for an opening statement?

THE COURT: I think it would help.

MR. HAIMOFF: Thank you.

If your Honor please, this action revolves around an investment made by the plaintiff in certain securities of The Firestone Group, Ltd. His investment was $510,000.

The investment was part of a private placement made by Allen & Co., under which the securities were sold, I believe, to approximately twenty or twenty-two investors. The transaction, the investment which the plaintiff made, took the form of a note and stock purchase agreement. That is, the transaction involved $250,000 worth of notes and five thousand shares of stock. The total purchase price of each unit was $255,000, and the plaintiff acquired, under circumstances which are not really important at the moment, two units, for a total investment of $510,000.

266a-2

What is important and what goes to the heart of the case, I believe, your Honor, is an unaudited financial statement which was annexed to the note and stock purchase agreement, which indicated that this corporation had earned a profit, deferred and realized, of approximately $1.3 million. The precise figures are stated in the unaudited financial statements.

Part of the transaction was a commitment by Firestone to furnish each of the investors with an audited financial statement for the purpose of confirming the unaudited figures which were part of the note and stockpurchase agreement.

The note and stock purchase agreement -- and I think this fact is significant, your Honor, is dated November 10 1969. The audited statement was prepared and issued by the defendant Laventhol firm, and it is dated December 5, 1969. That statement substantially confirmed the unaudited financial figures. As a matter of fact, where the unaudited figures had indicated deferred income of $1.3 million, the Laventhol statement showed deferred profit of $1.7 million or, rather, $1,700,000.

So that, if anything, what Laventhol did was to fortify the impression which any investor would get, which was this was a very profitable enterprise.

266a-3

Now we get to, as I say, the heart of the case. The profit was predicated upon one transaction -- and this, of course, is fully set forth in the work paper of Laventhol -- one transaction, which involved the purchase by Firestone of twenty-three nursing homes from a concern, an Ohio corporation called Monterey. The contract covering that alleged purchase was dated November 22, 1969, and that was their investment, and in that transaction they made an investment, according to the contract, of over $15,000,000.

The only cash outlay -- and this was all clearly set forth in the work papers, the Laventhol work papers -- was a $5,000 deposit. That was one part of the transaction. The other part of the transaction was a sale, supposedly, four days later of the very same properties to a company called Continental Recreation Company, the president of which was a person named Max Ruderian. Under that contract, the properties were sold to Continental Recreation for over $15,000,000, so that the apparent gross profit on the transaction was over $2,000,000, but the total investment by Firestone was $5,000, and the total investment by Continental was $25,000.

So that in a transaction where all that was put up on one side was $5,000 and all that was put up on the other side was $25,000, Firestone purported to show a profit of

$2,000,000.

Now, what impression ought that to create upon accountants coming in to audit the books of the company, and, as they have conceded or admitted -- as they have conceded -- that they knew their statement was to be used in order to sell securities of Firestone.

Bear in mind that the stock purchase agreement is dated November 10th. This transaction is not reflected anywhere on the books of the corporation, except in one minor respect. There is a reference to a $25,000 cash deposit under the caption "Exchange". That is all that the books of the corporation say about this $13,000,000-$15,000,000 transaction. That is all the books said about the $2,000,000 profit.

1 pm

Now, what company was Continental Recreation, according to the testimony given by one of the defendant's representatives? Continental owned miniature golf courses and had a net worth of $100,000, so this didn't have anything of substance to the transaction.

Then, if you look at the contracts themselves, your Honor, these contracts, incidentally, your Honor, I have taken from the work papers of Laventhol. They were not prepared by attorneys. They don't describe the property except by some name. They say that the properties are situated in various counties and states as per Exhibit A.

Here is Exhibit A. No reference to any county, no reference to any state, and the same thing is true of the contract of sale to Continental Recreation.

As a matter of fact, there is a significant typographical error; one of the hospitals is listed as Nashville in the purchase agreement and as Ashville in the sales agreement. In this multimillion dollar transaction, nobody took the trouble to read proof on the exhibits, so that they would be buying and selling the same hospitals.

Now, they were selling supposedly hospitals. There is no reference to any equipment, any licenses, no representations, no warranty. Our contention is, your Honor, that --

jb-2

266a-6

THE COURT: I thought you said they were selling nursing homes.

MR. HAIMOFF: Nursing Homes or hospitals. They are referred to variously in the records.

Now, the contracts themselves indicate that they are not contracts of sale whereby the plaintiff acquired title, whereby Firestone acquired title or Continental REcreation acquired title. They make very clear that all that was involved was an option on the part of the plaintiff to purchase -- on the part of Firestone to purchase, and on the part of Continental to buy.

The specific provision in the agreement is that "buyer reserves the right at any time after January 30, 1970, or upon payment of the $3,970,000 cash down payment as required herein to convert this contract of sale to a conventional sale, at which time title shall pass to buyer."

So that, therefore, Firestone did not have title to the property when this contract was executed, nor did Continental acquire title to theproperty when it executed its so called sales agreement.

Nevertheless, despite those circumstances, Laventhol did not call upon counsel for the company to ask whether those contracts were enforceable agreements, whether title had passed, whether or not the provisions

for the description of the various properties being sold was sufficiently definite nor did they ask for an opinion of counsel to certify as to the validity and or the enforceability of these agreements, and under the circumstances where it was obious that Firestone needed a substantial transaction and a substantial profit to show a presentable statement, and bearing in mind that this transaction involved sales of 15 million, whereas the gross sales of Firestone were 22 million, so you were dealing with 15 out of 22 million dollars and if you did not include this transaction, and there is no dispute about this, if you did not include this transaction in the audited figure, the company would show a loss.

Knowing all this, the accountants made no effort at any significant verification of the transaction.

There are other documents which throw further suspicion on the transaction. On November 10, the transaction is in effect projected. Up to that point, there is not a scrap of paper in the files of Firestone to indicate that any such transaction occurred.

And here, I think, is one of the most significant memoranda in the case. On November 21, the day before the contract between Firestone and Monterey is executed, a memorandum is prepared by a Miss Amberson, who is an employee,

not an officer, of the company in which she says that we have entered into -- we have entered into a contract to purchase these hospitals, have entered into a contract to sell these nursing homes, I should say. The purchase price, she says, and this is now on November 21, the purchase price is 10 million and the sales price is 11 million four hundred thousand.

So that, between November 21, this memorandum, prepared by an employee, which is put into the file for I have no idea what reason, you would have thought that a transaction which represented 70 or 80 percent of the total transactions of the company, total sales of the company, would have been handled by the president or an officer of the company, is in effect being handled by a person who I believe is an assistant to one of the officers, a lady, Miss Amberson, and she says that the transaction involved a $10,000,000 purchase, an eleven point four hundred thousand dollar sale and, overnight, between November 21 and November 22and November 26, the contract involves 13 million and 15 million.

So, it would seem to me, your Honor, that there is ample evidence here to show that at the very least the accountants were put upon inquiry as to the genuineness of this transaction and that they should have had something in

their filed which would indicate some opinion of counsel, some even written confirmation from Continental, which they didn't have, and this is another interesting phase of the case:

The only confirmation that they did as to Continental was to call them on the telephone, a friend of his called him on the telephone in the presence of the accountant, who was in charge of the audit, and they asked him whether or not he intended to go through with the deal and he said he did.

Now, there is other evidence that Firestone, the president of this company, and Ruderian have known each other for a long time. As a matter of fact, Firestone himself prepared a memorandum in which he says that the practice that, the Ruderian practice is to buy and sell before he closes title. So, this was another factor which should have lead the accountants to wonder whether or not this was a genuine transaction and whether they had a right to render any opinion at all.

Then there is something else involved. The contract which has been executed by Continental provided for liquidated damages in the event that title didn't pass or they didn't close the transaction of $185,000 and also Continental had paid $25,000 as a deposit and was to pay

another $25,000 in January.

So, the accountants included $50,000 -- the two $25,000 payments -- $185,000, the liquidated damages provision, in earned, realized income for the period ending November 30, 1969.

Now, that $235,000 income was essential to turn the income figures, the realized income, now, from a loss to a profit. If it hadn't been for that $235,000 profit which they picked up in their audited November 30, 1969 figures, the net realized income of Firestone would have shown a deficit.

So, on the one hand, they included in sales $15,000,000 -- 15 out of 22 million -- they included that in sales, which is obviously on the theory that the transaction will close, and in profits they included $185,000 in liquidated damages, which were on the theory, obviously, that the transaction would not close.

So that you have here a transaction, your Honor, in which an accountant is called upon to review the accounts of a company, knowing that the company is about to sell securities, knwoing that there is no evidence or any record of this multimillion dollar transaction at the time they begin their audit and before they finish their audit, all of these records suddenly appear, on November 21, 22, 26.

They get no attorney's opinions; they don't even bother to inquire whether Firestone has had a director's meeting at which these purchases and sales have been approved; they just gullibly accept whatever they are told. They adopt different theories, inconsistencies with profits on the figure on sales and they render their auditor's report.

Now, of course, your Honor, they were concerned about this; there is no doub- about it. They knew full well what they were doing and that's clear from the report which they submitted and a note which they added to the financial statement.

They rendered what may be called a qualified opinion. They said that their examination has been in accordance with accepted accounting procedures and standard or accepted accounting principles, except subject to the collectibility of the balance receiveable on the contract of sale. That was the exception which they included in their certified report.

Now, the balance receiveable would not be an obligation of Continental unless it elected to go through with the deal. Obviously, if it chose not to go through with the deal, its only responsibility was to pay $185,000 in liquidated damages, which they had really already picked

in income.

So, my contention is, as to this so-called exception, that it further fortifies the misleading nature and the incorrect nature of the report. It suggests as collectible as an obligation of Continental. Of course, they can't say whether it is collectible or not because, obviously, the company has a net worth of $100,000, so they think to protect themselves with this exception, but at least it assumes an obligation to pay it and how anybody could determine, any investor could determine what investigation they made as to the collectibility of this amount or why there was a question about it, there is nothing in here which says that Continental Recreation has a net worth of $100,000 and owns a few miniature gold courses and, more than this, they knew, according to the conversation with Ruderian, that he had discussed the venture with certain people in Hawaii and they were going to put up the money.

THE COURT: I don't want to interrupt you but I have another matter that takes some urgent attention. If you are going to be a few minutes, all right, but if you are going to go on --

MR. HAIMOFF: I think I will only be a few minutes, your Honor.

THE COURT: All right.

MR. HAIMOFF: So that what they are told conflicts with everything, what Ruderian tells them is in conflict with everything that Firestone told them and is in conflict with everything they said in the report.

In the report, they are in effect saying that Continental is going to pay the money. They were told that he was looking to resell the venture to some Hawaiian investors. They had no idea whether he had closed any such transaction, whether he had any commitment from the Hawaiian investors to do anything but, nevertheless, they went ahead and issued the statement.

In Note 4, a whole page long, and which sets forth all of the terms of both these pu-chases and sales transactions, they simply itemize the details of the transaction and they say, and here is another, I believe, flat misstatement, that Firestone has acquired these properties; Firestone had acquired exactly nothing. Firestone had put up $5,000. Firestone had the right to acquire the properties if they put up another $3,700,000. They hadn't done so and they would have a right not to do so and, as a matter of fact, they didn't do so and nothing else happened and I don't have to add, your Honor, that when the time came for Continental Recreation to close the deal,

SOUTHERN DISTRICT COURT REPORTERS
UNITED STATES COURT HOUSE
FOLEY SQUARE, N.Y., N.Y. 10007 TELEPHONE: CORTLAND 7-4580

it didn't do it.

And, Firestone sends a report to its stockholders and says, "Well, Continental is not going ahead with the deal and I have extended his time to July, and in the meantime I will sell it to somebody else," which again fortifies the palpable fraud that was committed.

One further point and then I will be through.

One point that I believe the defense will rely heavily upon is the fact that the plaintiff, Gerald Herzfeld, testified at pretrial and will undoubtedly testify here, that he didn't look at the report which was the qualified report and he didn't look at the note. All he looked at was the income statement.

Well, our position with respect to that, your Honor, is very simple. We claim that if he looked at the note that would have further fortified his judgement that this was a solid, genuine transaction or that the profit was solid and genuine and if he had looked at the note, he would have assumed that the transaction had been consummated.

Therefore, all it would have done, had he looked at the report and at the note, would simply have fortified the overwhelming impression of profitability created by the unaudited figures and confirmed by the auditors figures.

THE COURT: I am sorry for the interruption.

MR. CRACO: Do you wish an opening statement from the defendant?

THE COURT: Yes.

MR. CRACO: Your Honor, I will be very brief and sketch the outline of the case as we see it.

We represent Laventhol, Krekstein, the accountants in this case.

When Gerald Herzfeld, the plaintiff in this case, first heard about the Firestone Group, whose financial statements are at issue here, it was from one David Baird, a broker in New York, unassociated with Laventhol, Krekstein, who came to him and told him that he knew of a private placement of securities, that it was the hottest thing that Charlie Allen had in his shop and that he ought to really participate in it.

Herzfeld was interested and pursued the matter further with Baird. I think the proof will show that in due course, when the transaction was consummated for the investment in what are called units, consisting in part of common stock and part of notes of Firestone, he did it in some arrangement of somewhat mysterious form with Mr. Baird.

In any event, his introduction to the transaction

was through Mr. Baird.

Thereafter, a gentleman by the name of Kramer, who was the son-in-law of Mr. Allen of Allen & Co., and his partner, came to dinner with Mr. Herzfeld and his wife, and, apparently not knowing that Baird had introduced the subject, again introduced the subject of the Firestone units to Mr. Herzfeld and did so again in enthusiastic terms and again touting it as something that was a hot item in Charlie Allen's then current portfolio.

Thereafter, Firestone, Mr. Herzfeld having expressed his interest in this matter, distributed a note and note purchase agreement, to which were attached certain unaudited financial statements. The document is dated November 10, 1969, and it reflects a very substantial net profit of some $700,000 and a gross profit of $1,300,000.

At this point in time, Mr. Herzfeld, by his testimony before trial, makes the decision to purchase the units, and he decides to purchase two units, either himself or through an investing partnership of which he was a part. Again, it is not clear that he was in fact the purchaser of all these securities, but, in any event, whoever purchased the securities in connection with the Herzfeld group purchased them on or about the 24th of November 1969, signed the not purchase agreement, and in the early part of December

transmitted two checks to the order of Firestone in an aggregate amount of $510,000.

All of that, all of that transpired on the basis of Mr. Baird's communications, Mr. Kramer's communications, the literature that was circulate by Firestone and the unaudited statement, and before the Laventhol audited statements were transmitted to Mr. Herzfeld, which occurred on December 16, 1969, on December 16 or 17, 1969, after he had bought the units, he received the Laventhol statement.

His testimony before trial was that he did not read the audit report, that he read the accompanying letter, which emanated not from Laventhol but from The Firestone Group and purported to explain certain conservative changes that the auditors insisted on.

Having read that letter, his testimony is he glanced at only one of the seven pages of the audit report. That was the page reflecting the income statement, and on that page he looked at only one item: the profit item, by which he apparently means not the net profit but the gross profit.

An auditor's financial statement, an auditor's report on the financial statement of a company says on its face that it reports on the fairness and accuracy of the statement taken as a whole, that it adequately and fairly represents the financail statement or affairs of the corpora-

tion as of the time that it is published.

Mr. Herzfeld did not read the statement taken as a whole. He did not even read the report, the opinion of the auditor on which he here sues, because that report says on its face that it is qualified by being subject to the collectibility of the very transaction on which --

THE COURT: Do you say that personal reliance is necessary under the Securities Act?

MR. CRACO: Yes; I do. I think I have to make an important point here. This is a private placement. The stock is not publicly held. It is not publicly held here. This is not a class action. This is an action on a private investment by an individual who seeks redress for a single transaction.

It is our position that this transaction -- that his claim here, assuming that there was for the moment a a misrepresentation in the audit statement, which we won't concede for a minute -- assuming that we first of all insist that it was not in connection with the purchase or sale of any securities because the purchase of the securities had been accomplished prior to the time that the audit report was received.

Secondly, we take the position that he did not rely on it. It was not misleading to him, first of all,

he did not read it and was not misled by it, and, secondly, if he had read it and had seen the qualification on the face of it, if he had read the footnote which explains the transaction here involved, he would have gotten an adequate and full disclosure of all the matters he is entitled to know as a prudent investor.

We say, in short, that Mr. Herzfeld was not misled in the securities sense of this matter, first of all because he did not have the statement to rely upon when he made his investment decision and consummated it; secondly, when he got the statement, he did not read it. Had he read it, it would have accurately reflected the transaction.

As to that, I think we have to recognize if we do get to the point where proof is received with respect to the accounting treatment of the Ruderian transaction, that we are dealing with a fairly esoteric matter, which is the purchase and sale of California land under California law.

The transactions I think we can show, and I won't belabor the point at this point, were proper and enforceable transactions, entered into in accordance with the terms as at the date that they reflected; that they were the subject of a proper audit by Laventhol, including not as my brother has stated before a confirmation consisting of a check by a friend on the phone but an oral communication, an inquisition,

if you will, by a partner of Laventhol about the status of the contract and the foreseeability of its consummation.

Having adequately assured themselves that the transaction was a legal, valid and enforceable one in accordance with its terms, they took it into sales for that purpose and deferred the great part of the income, of the profit to be realized from that, beyond the date of which this report speaks.

It is the handling of that deferred income that makes the Laventhol statement actually very conservative, because what they did was, realizing the current period, only $25,000 that had been put up, $25,000 that was to be put up and $185,000 that would under any circumstances be realized as liquidated damages if the deal fell through -- they did this not in any sense inconsistently with having taken the sale into revenues but as a reasonable basis for evaluating what profit could be realized in the current term.

Had Mr. Herzfeld read the income statement of the Laventhol report with any attention at all, he would have seen that the net income reflected on the Laventhol statement was some $100,000 as against the $700,000 of net income which had been in the unaudited financials on which he did in fact rely.

In other words, the net income was down on the

audited statement some eighty per cent, and yet it is this statement that he said confirmed to him the profitability of the enterprise.

Your Honor, our case is simply that as a matter of law when the plaintiff's case is finished he will not have established the prima facia requisites of a 10b-5 action in this Court, because he will not have shown either the wrongdoing or the reliance thereon by Herzfeld or the requisite scienter or that it is in connection with the purchase or sale of securities.

If forced to our proof we will defend, I think adequately, the propriety of the audit steps and the accounting treatment accorded the transaction in the financials which Mr. Herzfeld did not read.

THE COURT: Mr. Pollack?

MR. POLLACK: If your Honor please, I represent four of the nine third-party defendants, Allen & Co., Allen & Co., Inc., Mr. Charles Allen and Mr. Irwin Kramer. Six other of the third-party defendants, so far as I understand it, were never served with process, and the ninth of the nine I believe was served, and I have no idea whether he is represented or not. That is Mr. David Baird. He is not represented by us, in any case.

THE COURT: Did you serve these other four

defendants?

MR. CRACO: Let me make a quick check, your Honor. Scott and Baird have both answered, your Honor. Scott has answered pro se and Mr. Baird is represented by, according to our records, Lawrence Brieant, Esq.

THE COURT: Are they here today?

MR. CRACO: Not to my knowledge, sir.

MR. POLLACK: In the original action or the third-party action, were they served with process?

MR. CRACO: If the Court please, I can get that. Do you want us to do that --

THE COURT: I want to clean this up. I don't want to have four trials or five trials. If they have been served where are they?

MR. CRACO: Baird answered in the third-party.

THE COURT: Are either of those parties here: themselves, that is?

MR. CRACO: Martin Scott answered in the third-party complaint on May 5, 1972. Mr. Baird answered by Mr. Brieant on March 27, 1972. Both are to the third-party complaints.

I might say, your Honor, from the time of joinder of issue to this date, so far as I know, there has been no action with respect to either of those defendants in the

third-party action.

All the pre-trial has gone on between Mr. Pollack, representing the clients he has identified, and ourselves.

THE COURT: Just a minute, Mr. Pollack. I want to know why they are not here. Probably my clerk did not notify them.

I will hear your opening. At the end of it, we will have to adjourn and get these people here.

MR. POLLACK: Your Honor, we see this action, if I may be permitted a characterization before I go into a brief statement of facts, as a case of a servile accountant, Lipkin of Laventhol, Krekstein, bending his will to the wishes of a promoter, Richard Firestone. The facts are relatively simple, and I do not think it will consume much time to recite.

Firestone Group, Ltd., a company which bore the name of Mr. Richard Firestone, was involved in the land business out in California. It had been organized, as I understand it, some time, I believe, in 1968.

In its second year of business, there came a point in time when it decided to effect a private placement. Allen & Co., Inc., is a well-known investment banking firm, as I think your Honor may know from newspapers and other matters, and Allen & Co., Inc. agreed to make a private place-

ment of $7,500,000 of the securities the Firestone Group lent them.

One of the ingredients of this private placement was to be a statement audited and certified by the accounting firm of Laventhol, Krekstein. The statement that was issued was issued dated December 6, 1969. The closing of the $7,500,000 transaction took place on December 16, 1969.

3A

In connection with that statement, we have essentially a company that had sales of approximately six million dollars. But the Laventhol statement doesn't show sales of $6,000,000. It shows sales of $21,000,000 or 22 million.

An important ingredient of that sale is that 15 of that figure is the $15,000,000 figure for the so-called sales to Continental Recreation of certain properties that they had allegedly bought from Monterey Nursing Homes for $13,000,000.

So, you have an inflated sales figure -- not just $6,000,000 but a $22,000,000 figure. You have an inflated profit figure both because of the liquidated damages figure that Mr. Haimoff mentioned in his opening and certain other reasons that are less central to the case, so that I will not get into them at this point with your Honor.

You also have a distorted balance sheet and income statement. But for this transaction and the inclusion of these liquidated damages into the income statement, the company would have shown a loss instead of a profit. But for the inclusion of this phony transaction which smelled like a dead fish, you would have had a company with sales of 6,000,000 instead of 22,000,000.

Our contention will be that Laventhol well knew

the shakiness of this transaction and they knew that the 15,000,000 sale had never been effected, despite what Mr. Craco says are the intricacies of California law. Laventhol knew that Firestone Group, Ltd., had not taken in that money, the $15,000,000, and yet they say in their financial statement, and I refer the Court to Note 4 , which is a critical part of this case: "The Firestone Group, Ltd., acquired" -- acquired in the past tense --"acquired by contract of sale, a group of convelescent hospitals containing approximately 1900 beds. The properties were leased back to the former owners. In November, 1969, the company sold"--past tense--"the properties by means of a contract of sale."

In fact, Firestone had never acquired these properties nor had Firestone sold them. This was a trumped up transaction for the purpose of making good this financial placement that they were about to engage in.

We believe that if we can get our witnesses from California here fast enough, before the end of this case, that we can show a pattern of secret meetings between Mr. Arnold Lipkin of Laventol, the west coast accountant, and Mr. Richard Firestone, the head of this company, aimed at improving the appearance of the financial health of this company.

In fact, we believe that we will be able to show that there were two December 6 statements, not just one, and

that the first one showed a considerably more qualified description of this phony Monterey Nursing Hospital transaction and that Mr. Firestone raised a fuss and Mr. Laventhol then pulled it out and replaced it with a more favorable statement, the statement that was ultimately given to Allen at the closing.

The net position in which we find ourselves is that Allen and Company, Incorporated, has for its own account $1,890,000 worth of these securities. There is no dispute that this financial statement was prepared by Laventhol for the use of Allen and I refer briefly to the testimony of Mr. Lipkin on that point, where he said in his deposition at page 31, "My understanding was that Exhibit 1, which is the financial statement, was to be furnished to Allen and Company in connection with our acquisition of their notes of the Firestone Company."

So that there can be no question but that Laventhol knew that this statement which they improperly put their seal of approval on was going to be used by the Allens in assessing whether the Allens would finally put their money into the Firestone Group.

There is one other very critical piece of evidence in this case, which bears on the relations between Mr. Lipkin of Laventhol and Mr. Richard Firestone and what these two

people were up to.

There is a memorandum dated December 2, 1969, written by Mr. Firestone to Mr. Lipkin, describing this Ruderian man and his company, the company to whom Firestone had allegedly sold $15,000,000 worth of hospitals, which he in fact didn't own. The closing paragraph of that memorandum I think sounds the bell for this case, as we see it.

I quote: "This man and his companies are very valued contacts...so if you speak to him, please handle him with kid gloves. We don't want to lose him for future transactions."

I think, your Honor, that the evidence will show that Laventhol improperly abandoned its professional posture and responsibility and bent its will to Mr. Firestone and put its seal of approval on a statement which created the impression of a company with $22,000,000 in sales, when in fact the company had $6,000,000 in sales and which created the impression that the company was making money when in fact it had lost money.

The Allens had no way to check this out independently. They had a right to rely on the auditor's statement.

In closing, I might add that this is not from our point of view a dispute between Mr. Herzfeld and Allen. Mr. Herzfeld has had his day in Court against Allen and that matter has been resolved. It is down now to the question of ultimate

liability and we feel the Allens are entitled to their money back from Laventhol as a result of the improper conduct of Laventhol in certifying this statement.

Thank you, your Honor.

THE COURT: We will take a very short recess until I see where these people are.

Do you press your action against these missing parties?

MR. CRACO: Reluctantly, I have to say I do. That is particularly true as far as Mr. Scott.

THE COURT: In that case, I have no choice but to adjourn until tomorrow morning at noon, here in this same room.

(Court adjourned until Oct. 15, 1973.)

GERALD L. HERZFELD

vs 71 Civ 2209

THE FIRESTONE GROUP, LTD., et al.

October 16, 1973
12:15 p.m.

(Trial resumed.)

Present: Mr. Haimoff
Mr. Craco
Mr. David
Mr. Pollack
Mr. Kaminsky
Mr. DeGaetano

- - - - -

THE CLERK: Attorneys for the plaintiff ready?

MR. HAIMOFF: Ready.

THE CLERK: Attorneys for the defendant Laventhol, Krekstein, Horwath & Horwath?

MR. CRACO: Yes.

THE CLERK: Are the attorneys ready for The Firestone Group, Ltd.?

(No response.)

THE COURT: Firestone? Who represents Firestone?

MR. POLLACK: They were never served.

MR. CRACO: Firestone was not served, your Honor.

THE CLERK: Allen and Company, Incorporated?

MR. POLLACK: Ready.

THE CLERK: Allen & Company?

SOUTHERN DISTRICT COURT REPORTERS
United States Court House
Foley Square, N.Y., N.Y. 10007 Telephone: CORTLAND 7-4580

MR. POLLACK: Ready.

THE CLERK: Charles Allen?

MR. POLLACK: Ready.

THE CLERK: Lee W. Meyer?

MR. CRACO: Mr. Meyer was not served.

THE CLERK: Irwin H. Kramer?

MR. POLLACK: Ready.

THE CLERK: Richard M. Firestone?

MR. CRACO: Firestone was not served.

THE CLERK: Martin A. Scott?

MR. CRACO: Scott was served and has joined issue.

THE COURT: Who represents him?

MR. CRACO: He appears in his answer in propria persona.

THE COURT: He was notified yesterday by telephone and by telegram to be here today for trial. He advised the Clerk that he was unable to come because he did not have the money to come from California; he can't afford it. He will therefore not appear for trial, unless the plaintiff pays the expense.

Does anyone want to pay his expense?

MR. CRACO: Not I, your Honor.

THE COURT: I didn't see anyone volunteering.

THE CLERK: David Baird?

MR. DeGAETANO: Your Honor, I am Peter DeGaetano, an attorney in the office of Lawrence Brinn, who appears for Mr. Baird.

I received a call from Mr. Brinn last night. I was not in the office yesterday. It was my understanding, and apparently erroneously, that this matter was on today solely for the purpose of picking a trial date.

THE COURT: I don't know where you got that understanding. You sure didn't get it from me or any member of the Court or any Clerk.

MR. DeGAETANO: I was not in the office this morning. I came from another Court. I don't even have the file with me.

THE COURT: You can work with somebody else's file. It's been in the Law Journal for some time, this case, and on the ready calendar and notified by telephone to be here.

MR. DeGAETANO: I just want it noted that I am completely unfamiliar with this matter.

THE COURT: You'll get familiar with it; so will I, I hope.

Let's proceed.

MR. HAIMOFF: Shall I proceed?

SOUTHERN DISTRICT COURT REPORTERS
United States Court House
Foley Square (N.Y., N.Y. 10007 TELEPHONE: CORTLAND 7-4580

THE COURT: Just a minute.

Do you wish to make any opening statement?

MR. DE GAETANO: Me, your Honor?

THE COURT: Yes.

MR. DE GAETANO: No, sir.

MR. HAIMOFF: May I proceed, your Honor?

THE COURT: Proceed.

MR. HAIMOFF: Mr. Gerald Herzfeld.

G E R A L D L. H E R Z F E L D, called as a witness and being duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. HAIMOFF:

Q Mr. Herzfeld, where do you reside?

A 812 Park Avenue, New York.

Q Are you the plaintiff in this action?

THE COURT: I'm sorry; I can't hear the witness.

Q Are you the plaintiff in this action?

A Yes, sir.

Q Do you recall that a time came when you made an investment in securities of a company called The Firestone Group, Ltd.?

A Yes.

Q Do you recall about when that was?

A I believe it was November, 69.

Q Can you tell me who it was who first called your attention to this investment?

A David Baird.

Q Who was Mr. Baird?

A Mr. Baird is a business broker and a friend of mine.

Q Can you tell us in substance what Mr. Baird said to you on this subject?

A Mr. Baird told me that he had had a call from Charles Allen, who advised him that he was making a private placement of some notes and stock and they were a very hot issue and offered Mr. Baird one unit.

MR. POLLACK: Your Honor, objection to the so-called conversation between Mr. Baird and Mr. Allen. It is hearsay.

THE COURT: Sustained. Strike it out.

Q Did you thereafter enter into an arrangement with Mr. Baird?

A Yes.

Q Concerning your investment in the securities of Firestone Company?

A Yes.

Q I show you a paper and ask you whether you can identify it.

A Yes. This is an agreement between my brothers and myself with David Baird with respectto --

THE COURT: Sustained. It speaks for itself, doesn't it?

MR. HAIMOFF: Yes, your Honor.

I offer it in evidence.

THE COURT: Have you marked it?

MR. HAIMOFF: Mark it, please.

THE COURT: I asked you to mark your own exhibits, as you recall, at a pretrial conference. Each party mark his own exhibits. It saves a lot of time.

Plaintiff's 1 received.

Any objection?

MR. CRACO: No objection.

(Plaintiff's Exhibit 1 received in evidence.)

MR. POLLACK: May we see the document, please, that you are marking?

(Document handed to Mr. Pollack.)

MR. HAIMOFF: Shall I proceed, your Honor?

THE COURT: Proceed.

Q Did you subsequently receive from the Firestone Group Ltd. a note and stock purchase agreement?

A Yes.

Q Was that transmitted to, that agreement, in a letter?

A Yes.

Q I show you a paper and ask you whether that is the letter that you received from the Firestone Group, Ltd.

A Yes, it is.

MR. HAIMOFF: I offer it in evidence.

THE COURT: Have you marked it?

MR. HAIMOFF: No, your Honor. Your Honor, I don't recall that there was a pre-trial conference.

THE COURT: There was a pretrial conference, and I directed that exhibits be marked. At least mark them now. Just put "Plaintiff's 2" on it.

MR. HAIMOFF: All right.

MR. CRACO: Excuse me, is this the original?

MR. HAIMOFF: No, this is the only copy that I have.

Whether it's an original or a copy --

MR. CRACO: It's the same one that was marked on the deposition?

MR. HAIMOFF: Right.

MR. CRACO: No objection.

THE COURT: Show it to Mr. Pollack.

MR. HAIMOFF: Beg your pardon?

THE COURT: Show it to all your adversaries.

MR. POLLACK: No objection.

(Plaintiff's Exhibit 2 received in evidence.)

Q Did you subsequently execute a note and stock purchase agreement?

A Yes.

Q I show you a paper entitled"Firestone Group, Ltd. Note and Stock Purchase Agreement," and ask you whether thatis the agreement that you executed.

A Yes.

MR. HAIMOFF: I offer it in evidence.

THE COURT: Let me stop this right now. Is there any dispute about these underlying agreements? Does anyone contest them?

MR. HAIMOFF: I don't know, your Honor. I tried to stipulate certain of these things with Mr. Craco, but he was not willing to.

THE COURT: Is there any contest about it?

MR. CRACO: I don't know what you are asking is there any contest about. Is there any contest about --

THE COURT: These documents.

MR. CRACO: -- about the execution of these agreements? No, sir, there is not. There is a lot of dispute about the origin of this investment, and I am perfectly willing to allow the exhibit to go in, and I haven't objected to it.

THE COURT: You should have stipulated it. We have other things to do than to sit up here spinning our wheels.

MR. CRACO: If your Honor please, I was not asked to stipulate to it.

THE COURT: I will recess. Sit down and stipulate all of this. I am not going to sit here while we go through this. I am too busy.

MR. CRACO: Your Honor, there was no pretrial conference in this case.

THE COURT: Well, hold one.

MR. CRACO: So wehaven't had the opportunity.

THE COURT: Well, hold one now and stipulate all of this. We will adjourn until 2:15. Sit down and see if you can stipulate all of these things. We can move along to the issues in the case.

(Luncheon recess.)

AFTERNOON SESSION

2:45 p.m.

(In the robing room.)

THE COURT: Mr. Baird, I understand your lawyer has left.

MR. BAIRD: Well, he couldn't be here this afternoon but I will go ahead without him. I will take the responsibility. I told him as long as he was otherwise engaged -- you see, I only knew about this yesterday.

THE COURT: I apologize for the fact that you got short notice, but --

MR. BAIRD: I'll do the best I can. You can go at me any way you want.

THE COURT: We have another problem, so that we are going to adjourn this case now until Thursday at noon.

Would you tell your lawyer to be here. If he is not, of course, you have the right to proceed without him but, Thursday in this same room at noon.

MR. BAIRD: I'll be here, sir.

THE COURT: All right. I just wanted you to know that.

MR. BAIRD: Thank you, very much. Glad to see you all. Goodbye.

THE COURT: In the meantime, I hope that the rest

of you will try to work out a pretrial order that you can present to me Thursday morning, and I will direct the Clerk to send another telegram forthwith to Mr. Scott, advising him that, to suit his convenience, we are adjourning the case until Thursday at noon.

(Trial adjourned.)

SOUTHERN DISTRICT COURT REPORTERS
United States Court House
Foley Square, N.Y., N.Y. 10007 TELEPHONE: CORTLAND 7-4580

WITNESS INDEX

Name	Direct	Cross	Redirect	Recross
Gerald L. Herzfeld	33			

EXHIBIT INDEX

Plaintiff	Identification	In Evidence
1		35
2		37

UNITED STATES DISTRICT COURT REPORTERS
FEDERAL BUILDING AND U.S. COURT HOUSE
FOLEY SQUARE, NEW YORK, N.Y. 10007 TELEPHONE (212) 791-1020

GERALD L. HERZFELD
vs. 71 Civ 2209
THE FIRESTONE GROUP, LTD.,
et al.

New York, October 18, 1973.

Present:

Mr. Haimoff.
Mr. Craco.
Mr. David.
Mr. Pollack.
Mr. Kuminsky.
Mr. Brinn.
Mr. Scott.

- - -

THE CLERK: Plaintiff ready?

MR. HAIMOFF: Plaintiff ready.

THE CLERK: Defendant ready?

MR. CRACO: Defendant ready, your Honor.

THE CLERK: Allen & Company, Inc.

MR. POLLACK: Ready.

THE CLERK: Charles Allen?

MR. POLLACK: Ready.

THE CLERK: Irwin H. Kramer?

MR. POLLACK: Ready.

THE CLERK: Martin A. Scott?

MR. SCOTT: Ready.

THE CLERK: David Baird?

MR. BRINN: Your Honor, I would like to talk

for a second, your Honor. I am Mr. Brinn. I have represented Mr. Baird in this matter, and it was, in my understanding, just a token representation of putting an answer in. We have not participated in any of the proceedings, in any of the examinations, and I ask to be withdrawn from the case, and Mr. Baird would like to carry it on himself.

We have not received any fee --

THE COURT: I am sorry, your application comes much too late. You are in the case. I am not going to let you out when the case is called for trial, sorry.

MR. BRINN: I do want to say one thing more. We have not received any fee, and we do not plan to.

THE COURT: I can't let you out of the case. You have represented him since 1971, and this is the time when it is called for trial, and I cannot do it, and I won't do it.

MR. BRINN: We do not attend in litigation courts, your Honor, and we have no one in the office to do it, just myself and Mr. De Gaetano.

THE COURT: I am sorry, you will have to do it. I am sorry, that is it.

MR. BRINN: And Mr. Baird himself --

THE COURT: Please don't press it any further.

Come up to the counsel table. You are appearing in this action. Come up here, and take Mr. Baird with you if you want him.

All right. Now, Mr. Scott, before you rise, I might explain to you the reason you were not notified earlier was unfortunate, the docket sheet said that you had no address, gave no address. For that reason you were not notified earlier, and the trial commenced Monday in your absence.

We didn't get very far. The transcript of the proceedings that occurred in your absence is available, and you may see it if you wish to do so. All that happened was that counsel had made their opening statements and started to adduce some of the basic agreements that are involved.

If you wish to make an opening statement of any kind I would be happy to hear it now.

MR. SCOTT: I will reserve it.

THE COURT: All right, we will proceed.

MR. HAIMOFF: If your Honor please, at the Court's suggestion, we had the opportunity yesterday and the day before to work out a pretrial order which I have in my hand. Mr. Craco and I have executed it. Mr. Pollack is now reading it, I think it's fair to say, for the first time, so as soon as he had an opportunity to read it,

we will offer it in evidence as soon as he approves it, subject to whatever revisions he has.

THE COURT: Of course, the other partieshave to approve it as well, Mr. Baird and Mr. Scott.

MR. HAIMOFF: That is true, your Honor. I hadn't thought of that.

MR. POLLACK: Your Honor, I did not receive a copy of this, but --

THE COURT: I understand. It was done on short notice.

MR. HAIMOFF: Right.

THE COURT: Save the time of telling me you didn't receive it by reading it.

MR. POLLACK: I have read it. I am perfectly prepared to accept the points II and IV which I suggested to Mr. Craco yesterday in writingand to Mr. Haimoff. Parts I and III deal with the Haimoff-Craco trial and not ours, so as to those I would have no comment and would not stipulate because I have no basis for doing so.

THE COURT: I see, but you have no objection?

MR. POLLACK: No.

MR. HAIMOFF: With that understanding on the record, shall we offer it up, your Honor?

MR. POLLACK: There is one additional page of

exhibits that we intend to offer which should be added to IV, which I can hand to all counsel.

THE COURT: All right, do that, Mr. Pollack.

MR. POLLACK: And they will be deemed part of IV.

MR. CRACO: Mr. Pollack, if I may, your Honor, is that the copy that was handed to us this morning?

MR. POLLACK: Yes, Mr. Craco.

MR. CRACO: I have no objection to including that.

MR. HAIMOFF: I have no objection. Mr. Scott is reading it.

MR. CRACO: If the Court please, while Mr. Scott is reading that pretrial order, may I ask leave to hand up to the Court for its convenience a set of marked pleadings in the third-party action. My understanding is that Mr. Haimoff has marked pleadings in the action in chief.

THE COURT: Do you?

MR. HAIMOFF: Yes, sir, I have.

THE COURT: May I have them?

MR. CRACO: They have been handed up on the first day.

THE COURT: I see. All right.

MR. CRACO: Your Honor, in the light of the question you addressed to me in the opening statement, I would like leave to hand up a short supplemental trial brief on the point of reliance and causation. Mr. Haimoff, I will be glad to give you a copy of it.

MR. HAIMOFF: Shall I proceed, your Honor?

THE COURT: Why don't you offer the stipulation?

MR. HAIMOFF: If your Honor please, I offer the stipulation andthe pretrial order which has been consented to by myself as attorney for the plaintiff, by Mr. Craco as attorney for the defendant Laventhol, and which has the approval of Mr. Pollack as the attorney for the Allen defendants in the form in which he has stated it on the record.

THE COURT: Does anyone have any objection? Mr. Scott?

MR. SCOTT: No.

THE COURT: Mr. Baird, do you have any objection?

MR. BRINN: We haven't seen it, sir.

THE COURT: Show it to them.

MR. BRINN: I want to state that I saw the stipulation for the first time and I read the parts and paragraphs as they referred to Mr. Baird to him, and asked

him to his best recollection were they accurate statements, and he says, "I believe they are accurate." That is the best he could recall at this time.

THE COURT: All right.

MR. BRINN: The other statements there I have no knowledge of.

THE COURT: All right, we will receive it.

MR. BRINN: I would like a copy.

THE COURT: If there is any argument you want to make later about any of it, you may.

All right, let's proceed.

MR. HAIMOFF: May I proceed, your Honor? Mr. Herzfeld.

G E R A L D L. H E R Z F E L D, the plaintiff, having been previously sworn, resumed, and testified further as follows:

DIRECT EXAMINATION CONTINUED

BY MR. HAIMOFF:

Q Mr. Herzfeld, I show you a paper which has been marked Plaintiff's Exhibit 3 entitled "The Firestone Group, Ltd., Note and Stock Purchase Agreement," dated November 10, 1969, and ask you whether or not you read that document when you executed it or prior to the time you executed it.

A Yes, I did.

Q I call your attention to Exhibit B annexed to the agreement which has been marked Plaintiff's Exhibit 3, and ask you whether you can tell me whether or not you read any part of that exhibit.

A Yes, I did.

Q Which part did you read?

A All of it.

Q Bearing in mind, Mr. Herzfeld, that Exhibit B contains a balance sheet as well as an income statement, is it your testimony that you read both the balance sheet and the income statement?

A Yes.

Q With respect to the income statement, were there any figures included on the income statement, which is part of Exhibit B, to which you paid particular attention?

A Yes, sir, I paid particular attention to the income statement.

Q And what did the income statement indicate to you?

A It indicated to me that this was a very profitable company and that the earnings were, oh, approximately $2 a share for the period ending November 30, 1969.

Q Now, based on that information, did you arrive at any conclusions as to the value of the Firestone stock?

A Yes, I did.

Q And what was that?

A At this point, I attributed to the Firestone stock a value of approximately ten times earnings, or approximately $20 a share.

Q Mr. Herzfeld, I show you a paper which has been marked Plaintiff's Exhibit 2 and which purports to be a letter dated November 21, 1969, addressed to you on the letterhead of the Firestone group, and I ask you whether you read that letter when you received it?

A Yes, I did.

Q Now, do you recall whether or not you observed, in reading that letter, any reference to audited statements?

MR. CRACO: I am sorry, your Honor. May I hear that question?

(The question was read.)

MR. CRACO: I object to the question. The document

2 gwrf Herzfeld - direct

speaks for itself.

MR. HAIMOFF: May I be heard, your Honor?

THE COURT: Yes.

MR. HAIMOFF: Since one of the principle issues in the case is the issue of reliance, it seems to me relevant to call the Court's attention not only to the documents but to the facts as to what attention, if any, he paid to them. It is for that purpose that I ask that question.

THE COURT: I suppose you can establish that if you show he read it.

MR. HAIMOFF: Very well, your Honor.

Q You testified, then, Mr. Herzfeld, you read this letter when you received it?

A Yes, I did.

MR. POLLACK: Could he speak a little louder. It is very difficult to hear.

THE COURT: Move a little closer. The acoustics are terrible. This room would make a better basketball court than a courtroom.

MR. CRACO: I am not sure I know what the present status of these exhibits are. We have marked them on the pretrial and I don't know that they have been formally tendered in evidence.

THE COURT: You can tender them in evidence.

gwrf 3 Herzfeld - direct

MR. HAIMOFF: They are referred to in the pretrial order.

MR. CRACO: We stipulated that to the great bulk of them but not to all of them.

THE COURT: To make doubly sure, offer them in evidence.

MR. CRACO: I have no objection to exhibit which we were offered first and Exhibit 2.

MR. HAIMOFF: I offer Plaintiff's Exhibit 3 and Plaintiff's Exhibit 2 in evidence.

THE COURT: Received.

(Plaintiff's Exhibits 2 and 3 received in evidence.)

xx

Q Mr. Herzfeld, I show you a letter dated December 16, 1969, on the letterhead of the Firestone Group Ltd. addressed to you which has been marked Plaintiff's Exhibit 6 and ask you whether you received that letter on or about the date that it bears?

A Yes, I did.

Q And did you read the letter?

A Yes, I did.

Q When you received it?

A Yes, sir.

MR. HAIMOFF: I offer it in evidence.

MR. CRACO: No objection.

gwrf 4 Herzfeld - direct

THE COURT: Received.

(Plaintiff's Exhibit 6 received in evidence.)

Q Now, Mr. Herzfeld, in Plaintiff's Exhibit 6 do you observe that reference is made to audited financial statements?

A Yes.

MR. CRACO: Objection, your Honor.

MR. HAIMOFF: I beg your pardon?

MR. CRACO: I object.

The document speaks for itself.

MR. HAIMOFF: It is for the sake of continuity.

MR. CRACO: I will withdraw the objection.

Q I show you a report which purports to be a Laventhol report which has been marked Plaintiff's Exhibit 7 and ask you whether you received that report on or about December 16, 1969?

A Yes, I did.

MR. HAIMOFF: I offer it in evidence.

MR. CRACO: I have no objection to its receipt in evidence as a document received by Mr. Herzfeld on or about that date.

THE COURT: Received.

(Plaintiff's Exhibit 7 received in evidence.)

gwrf 5 Herzfeld - direct

Q Now, Mr. Herzfeld, can you tell me whether or not you read that report at the time you received it?

A When I received this report I opened to the income statement. That's the only portion of the report that I recall reading.

Q Are there any figures on the income statement --

MR. HAIMOFF: Which, your Honor, I have marked Plaintiff's Exhibit 7-A.

Q -- to which you paid particular attention at that time?

A Yes, I paid particular attention to the earnings as indicated on the income report.

MR. CRACO: If the Court please, may we for purposes of identifying it with particularity have the witness read the line to which he is referring?

THE COURT: I think it would help.

MR. HAIMOFF: I might be met with an objection that the document speaks for itself.

Thank you.

THE WITNESS: I was particularly impresssed with the gross profit -- the deferred gross profit of $1,795,000.

MR. HAIMOFF: I think for purposes of continuity, your Honor, I would like to call the Court's attention to the fact that Plaintiff's Exhibit 9, which is an annual

report to shareholders, states that the transaction which is discussed in that report and which we have referred to as the Monterey transaction was not consummated in January of 1970.

THE COURT: Not consummated.

MR. HAIMOFF: Was not consummated.

MR. CRACO: If your Honor please, Exhibit 9 hasn't even been offered in evidence and now counsel is characterizing its contents.

THE COURT: Let's not characterize it. Let's get the proof in. I will give you an opportunity to argue it and we have it into what pattern of proof you think you have shown.

MR. HAIMOFF: I would like to read to the Court one or two sentences from this report which relates to the point that I made.

MR. CRACO: Your Honor, I will stipulate that that document was received by Mr. Herzfeld on some date.

THE COURT: Offer it in evidence, will you? I can read it and will in the proper time.

MR. CRACO: Excuse me, your Honor. Our stipulation, and I think Mr. Haimoff will bear me out on this with respect to this exhibit, was that it was received after any pertinent date in this litigation and that I was prepared to stipulate

to its admissibility solely for the purpose that Mr. Herzfeld received it on or about a date that Mr. Herzfeld was supposed to tell us about in open court. Mr. Haimoff was supposed to adduce that date because he didn't know it when we sat down to the pretrial.

THE COURT: In the shorthand of lawyers I gather your objection is it is immaterial.

MR. CRACO: It is immaterial and unauthenticated at this point.

THE COURT: Have you offered it? Offer it and let him make his objection and then I can rule.

MR. HAIMOFF: Thank you, your Honor.

I offer in evidence as Plaintiff's Exhibit 9 a document which purports to be an annual report to shareholders, 1970.

MR. CRACO: May I have one question on the voir dire?

THE COURT: Yes.

VOIR DIRE EXAMINATION

BY MR. CRACO:

Q I show you Exhibit 9 for identification, Mr. Herzfeld, and I ask you if you received that document?

A Yes, I did.

Q Do you know when you received that document?

A I don't recall.

Q Would you look at the date of the document?

MR. HAIMOFF: We agree it was not received until sometime late in May.

MR. CRACO: Let's establish the record, if I may.

MR. HAIMOFF: I have no objection.

A What is your question?

Q Look at the document.

A It says annual report to shareholders, 1970.

Q Does it contain a letter to shareholders from the president and does that letter to shareholders on the fourth page of Exhibit 9 bear the date May 28, 1970?

A Yes, it does.

Q And did you receive it on or after May 28, 1970?

A I don't recall when I received it.

THE COURT: Does that help refresh your recollection?

THE WITNESS: No, your Honor.

MR. CRACO: I object to its admissibility.

MR. HAIMOFF: For the purpose of the record I would be very glad to stipulate, your Honor, that the document was received after May 26th or May 28, 1970.

MR. CRACO: I object to its materiality and relevance but I will stipulate that it was a document received by Mr. Herzfeld after that date for whatever that

gwrf 9 Herzfeld - direct

may be worth.

MR. HAIMOFF: May I be heard on the question of relevance.

THE COURT: Yes.

MR. HAIMOFF: The document is offered for one purpose exclusively, and that is to establish that the so-called Monterey transaction was not consummated in January of 1970.

THE COURT: All right, we will take it for that limited purpose.

(Plaintiff's Exhibit 9 received in evidence.)

BY MR. HAIMOFF:

Q Mr. Herzfeld, other than the securities, the Firestone securities, in which you invested which are involved in this case, have you from time to time made investment in other securities?

A Yes, I have.

Q And have you invested in a list of securities?

A Yes, I have.

Q Now, in making your investments in the securities in which you invest, what criterion or criteria do you employ?

A Essentially a price/earnings ratio, earnings per

gwrf 10 Herzfeld - direct

share as related to the price of a stock.

Q And in making your decisions do you give consideration at any time to the balance sheet of the company?

A I would say no.

MR. HAIMOFF: I have no further questions.

MR. CRACO: May I briefly confer with Mr. Haimoff? It might cut things down, your Honor.

THE COURT: Surely.

(Counsel confer.)

CROSS EXAMINATION

BY MR. CRACO:

Q Mr. Herzfeld, I believe you testified yesterday that this matter was introduced to you, the Firestone underwriting was introduced to you by Mr. David Baird.

A That is correct.

Q Would you tell us, please, again in full substance what Mr. Baird said to you in the course of introducing that transaction to you?

A Mr. Baird told me that he had had a call from Mr. Charles Allen and that Mr. Allen had told him, Mr. Baird, that this was one of the hotest yields he had ever seen and wanted David Baird, who was his good friend, to have the advantage to participate in this deal.

Q Did he tell you anything else --

MR. POLLACK: Your Honor, objection, hearsay. The same alleged conversation was attempted to be testified to yesterday and I objected. Your Honor ruled it out.

MR. CRACO: May I be heard on that at this point, your Honor? I am not offering this testimony for the purpose of establishing that Charles Allen said that. I am offering it for the purpose of establishing that Mr. Herzfeld received that information, true or false, from Mr. Baird as going to Mr. Herzfeld's state of mind when he made the investment in issue.

THE COURT: The objection is overruled.

Q Did Mr. Baird say anything else to you about his conversation with Mr. Allen respecting the Firestone transaction?

A Mr. Baird told me that the company was very profitable, as I recall, and that with the additional seven and a half million dollars that was going to be raised in this private placement he looked forward to much greater earnings.

Q Did Mr. Baird tell you that of his own knowledge or did he report to you that he had received that information from someone else?

A No, I don't recall.

Q Specifically, did he indicate to you that Mr.

Allen had indicated to him that the company was very profitable?

A That was in 1969. I don't recall specifically, but I would think so.

Q What is your best recollection, sir?

A Well, I do not have a true recollection as to whether it was Mr. Baird's opinion or whether Mr. Allen had told Mr. Baird, but I would have to assume that Mr. Allen had told Mr. Baird inasmuch as Mr. Baird knew nothing more than what he reported to me about the company.

MR. POLLACK: Objection to what the witness assumed.

THE COURT: Yes. Strike it out.

MR. CRACO: Your Honor, at this point may I mark in its entirety as Defendants' Exhibit A the deposition of Mr. Gerald Herzfeld taken on April 5, 1970, in this proceeding?

THE COURT: All right.

Q As a preliminary to it I would ask, Mr. Herzfeld, whether on page 97A of this document your signature appears over the notary's certificate?

A Yes, it does.

MR. CRACO: May I offer it in its entirety, your Honor?

MR. HAIMOFF: Your Honor, I do not dispute the authenticity of the document nor the fact Mr. Herzfeld

gwrf 13 Herzfeld - cross

gave this testimony. I would like to reserve my right to object to any portion thereof as to its materiality.

MR. CRACO: It seems to me it would be a convenience to the Court since it is a relatively brief deposition to have it all before you because I am going to refer to parts of it from time to time as we go forward and it might be convenient for you to follow it.

MR. HAIMOFF: I have no objection to that procedure.

MR. POLLACK: We object to such portions as we objected to at the time of the deposition.

MR. CRACO: I offer it subject to those objections.

THE COURT: All right, I will take it subject to those objections. Any objections reserved at that time you may make at the appropriate time here.

(Defendants' Exhibit A received in evidence.)

xx

Q At page 49 of that transcript, on the occasion of that deposition, were you asked the following question and did you give the following answer:

"Q -- referring to line 2, Mr. Haimoff -- did you have confidence in David Baird's judgment? Did you rely upon his investment expertise?

"A I have confidence in David Baird but in this instance I had no occasion to rely on his expertise.

First of all, he professed ignorance about the entire situation except that which Charlie Allen told him. So he was scarecely in a position to use his expertise in determining whether or not this was a good investment. I did rely on my own limited expertise when you looked at the earning statement."

Did you give that answer to that question on that occasion?

A Yes, I did.

Q Does that refresh your recollection as to whether or not the information that Mr. Baird gave you about the profitability of Firestone was, according to Mr. Baird, derived from his conversations with Mr. Allen?

A Yes, it does.

MR. POLLACK: Objection.

Q With your recollection thus refreshed, would you tell the Court whether or not Mr. Baird attributed the information he had about profitability to Mr. Allen?

MR. CRACO: Again, your Honor, I am offering this solely for the purpose of identifying the source of his reliance.

MR. POLLACK: I continue my objection.

THE COURT: Overruled.

It is taken as to the state of mind.

A The answer is yes.

Q And did the fact that Mr. Allen, according to Mr. Baird, felt that this was a good investment and a profitable company play a part in your enthusiasm for the deal?

MR. HAIMOFF: I object to the word enthusiasm, your Honor.

MR. POLLACK: Objection, your Honor.

THE COURT: Yes, I think your question is bad in form.

Q Were you enthusiastic about the prospective investment after you finished talking with Mr. Baird?

A Yes, I was.

Q And in forming that enthusiasm, did the fact that Mr. Allen was of the view, according to Mr. Baird, that this was a profitable company and a good investment, play any part?

A I would think so.

Q Is it your recollection that it did?

A Yes.

Q Did Mr. Baird say anything to you in the course of that conversation about why he was tendering to you this investment opportunity?

A Yes, he did.

Q What did he say in that connection?

A He said that the unit would cost $255,000 and that the money had to be put up very shortly thereafter and he didn't have the funds readily available and, therefore, he offered a proposition to me whereby I would put the funds up and we would share in some form in the profit.

Q Did he identify the form in which he proposed that you share in the profit on that occasion?

A Yes, he did.

Q What was the proposition that he put to you?

A As I recall, he offered to take all of the losses and share the profits 50/50, and I gave him a counterproposition.

Q Excuse me. That was his proposition to you, is that right?

A That's my recollection, yes.

Q In other words, Mr. Baird's proposition to you on this occasion was that he was prepared to accept the entire downside risk in exchange for splitting the profits, if any, from the transaction on a 50/50 basis?

A That is correct.

Q Do you recall whether there was any conversation with Mr. Baird on that occasion about future prospects for the stock?

A Yes, there was.

Q Would you tell us in words or substance what you remember of that conversation?

A For each unit, and we were discussing one unit at the time, we were to receive 5,000 shares of stock. That stock was to be split two for one so that we would have 10,000 shares of stock, and we were to agree in the purchase agreement to sell 5,000 shares of the stock at $25 a share. We were obliged to do that.

Q Let me see if I understand this. Mr. Baird, as I understand your testimony, told you on the occasion of his first visit with you on this subject that the 5,000 shares would be split two for one, is that right?

A I am not sure if it was on the first visit or the second visit but that is the substance of the conversation.

Q Was it before you signed the purchase agreement?

A Yes, certainly.

Q Was it also your testimony that Mr. Baird on that occasion told you that upon the consummation of that split you would be obliged to sell back to Firestone 5,000 shares at a price?

A That is correct.

Q Do you recall what the price was?

A $25 a share.

Q And what was the price attributable to the stock

gwrf 18 Herzfeld - cross

as you were buying it in this private placement?

A After the split it would be 50 cents a share.

Q So Mr. Baird told you in the course of the first or second conversation you had about it that the prospect that the stock would be split two for one and for the 50 cents a share investment in the stock that you got you would be obliged to sell back the securities to Firestone for $25 a share to the tune of 5,000 shares, is that right?

A That is correct.

Q Did that play a part in what you now identify as your enthusiasm for the investment?

A Yes, it did.

Q Is it fair to say that that information from Mr. Baird filled you with confidence about the investment?

A It certainly encouraged me.

Q Did it fill you with confidence?

A I am not sure I would characterize it that way, but it certainly made me desirous to buy the stock.

Q On the occasion of your deposition were you asked these questions and did you give these answers, page 63, lines 4 and 5:

"Q Did David Baird tell you about this provision for splitting the common stock of Firestone when he first talked to you at your office in early November?

"A Yes, he did. And it filled me with confidence.

"Q Excuse me?

"A It filled me with confidence.

"Q What did he tell you about that?"

And the rest is not consistent.

Does that refresh your recolle[illegible]at in fact it filled you with confidence at that ti[illegible]

A What I just said to you is not inconsistent with that. I said I was enthused. Filled with confidence is substantially the same as I interpret it.

Q Did Mr. Baird tell you where he got the information about this stock split?

A I don't recall, but I would presume that he got the information from Mr. Allen.

Q Did he say he got it from Mr. Allen?

A I don't recall at this late date whether he said so, but I assume he did.

Q Did he tell you he got all his information from Mr. Allen?

A Yes, I believe he did.

Q Did he tell you he didn't know anything of his own knowledge?

A Yes, he did.

Q Is that the basis of what you have identified in

your prior answer as your presumption on the subject?

A That is correct.

Q Now, can you tell us about when this conversation, the first conversation, with Mr. Baird took place?

A I believe it was early November, 1969.

Q And the second conversation?

A A day or two later.

Q Who was present with you on the occasion of your first conversation with Mr. Baird?

A I don't know whether I met with Mr. Baird alone or whether one of my brothers was present or whether both of them were present.

Q How did it come about that you met with Mr. Baird at all?

A Mr. Baird telephoned me and said that he had a proposition he wished to discuss with me and asked if he could come up and if I could see him. I said with great pleasure.

Q And is it your best recollection and present testimony that the arrangement for this appointment was made by Mr. Baird for the explicit purpose of discussing this investment with you?

A Yes.

Q Would it refresh your recollection of I were to

ask you whether you had this conversation with Mr. Baird at a lunch?

A I don't recall whether we had lunch or whether we simply talked in the office.

Q Was Mr. Nathan Herzfeld present with you on that occasion?

A As I just testified, I don't recall if my brother was present or not present.

Q Nathan Herzfeld is a brother of yours?

A That is correct.

Q Now, did you respond to Mr. Baird's proposal to split the profits 50/50 for his assumption of the entire downside risk on the spot?

A I don't remember whether I gave Mr. Baird a counterproposition that day or the following day or a day later, but I did give him a counterproposition.

Q We will come to that. Let me ask you this preliminarily:

Between the time that you received the initial proposition and the time you made your counterproposition, did you discuss the initial proposition with anybody?

A If I did, I discussed --

Q Did you?

A I don't recall.

Q Did you discuss it with your brother?

gwrf 22 Herzfeld - cross

A I don't recall whether I did discuss it or I didn't, but I might very well have.

Q Did you fashion the counterproposal which you were about to describe in consultation with anybody?

A Probably in consultation with my brother.

Q Does that help refresh your recollection as to whether you talked to them about the subject?

A Well, I know I talked to them about the subject. I don't know whether it was on that specific day or not, Mr. Craco.

Q After the conversation with your brothers, to the best of your recollection, did you make this counterproposal to Mr. Baird?

A Yes, I did.

Q How did you communicate it to him?

A I don't recall whether Mr. Baird came to my office or we discussed it on the telephone.

Q What did you say to him and what did he say to you in the course of presenting that counterproposal to him?

A The essence of it was that I would bear the entire downside risk and Mr. Baird would share to the tune of 25 per cent of the profit with none of the downside risk.

Q And what did Mr. Baird say to that?

A Mr. Baird said that that was fine.

Q Did you state to Mr. Baird what reasons, if any, you had for your counterproposal?

A I don't recall whether I did or not.

Q Did you have any reason for your counterproposal?

A I didn't want --

Q Did you?

A The answer is yes.

Q What was the reason?

A I didn't want Mr. Baird to take the downside risk and for me to share 50 per cent of the upside risk.

Q Why?

A I felt that was unfair.

Q Why?

A As a matter of equity I thought it was unfair.

Q Was tha- the only consideration?

A The only consideration.

Q Was it not in fact also part of the consideration that you wanted 75 per cent of the upside risk?

A No, I don't believe so.

Q That played no part in your consultations with your brother?

A I dnn't believe so. I don't recall. It was four years ago. But I believe, as I stated a moment ago, I

felt it was unequitable for Mr. Baird to assume the entire downside risk and for me to still get 50 per cent of the profits.

Q But you were impressed, were you not, with Mr. Baird's willingness to accept the whole downside risk?

A Well, that is typical of Mr. Baird's exceptionally fair attitude about any proposition I have ever had with him.

Q And you were impressed by it?

A I have always been impressed by Mr. Baird.

Q You were impressed with Mr. Baird's willingness to accept the risk in this particular investment, were you not?

A I was impressed with Mr. Baird's willingness to always take the worst side of a deal.

MR. CRACO: I ask you direct the witness to answer the question.

THE COURT: I will come to that in judging the witness' credibility whether he is evasive or whether he is answering a question.

MR. CRACO: I have got as much as I want.

T3 Q All of these conversations took place, did they not, before you executed Exhibit 3 in evidence, the note and the stock purchase agreement?

A I believe so, yes.

Q Did they take place before you received the letter of November 21, 1969, which is Exhibit 2 in evidence?

MR. CRACO: Mr. Haimoff, may I have Exhibit 2 to show the witness?

THE COURT: Do you want an answer to the question?

MR. CRACO: I beg your pardon?

THE COURT: I didn't rule on your request for an answer to the question.

MR. CRACO: I would like an answer to the question.

THE COURT: Answer the question responsively.

MR. HAIMOFF: May we have the question read?

MR. CRACO: May I reframe the question, and I will try to do it --

THE COURT: Was he impressed with Baird's saying he would take half the downside risk?

MR. CRACO: All the downside risk.

A Yes.

Q Those conversations with Baird, did they take place before you received Exhibit 2 in evidence?

A Yes.

MR. CRACO: I don't want to root through your papers, Mr. Haimoff --

MR. HAIMOFF: What did you want?

MR. CRACO: Exhibit 3.

Q I take it from your prior answer that they also took place before you read Exhibit B to Exhibit 3 which are the unaudited financials as attached to the note and the stock purchase agreement; is that also correct?

A Well, certainly some conversations took place prior to receipt of this.

Q Did the two conversations you now identified with Mr. Baird take place prior to your receipt and study of Exhibit 3?

A Yes, they did.

Q Did you have any conversations with anybody else about the Firestone transaction prior to your receipt and execution of Exhibit 3 and your receipt of Exhibit 2?

A Yes, I did.

Q With whom did you have those other conversations?

A I had a conversation with Irwin Kramer.

Q Who is Irwin Kramer?

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Gerald L. Herzfeld,

Plaintiff,

-against-

Laventhol Krekstein Horwath & Horwath,

Defendant-Appellant.

Laventhol Krekstein Horwath & Horwath,

Third-Party Plaintiff-Appellant,

-against-

Allen & Company Incorporated and Irwin H. Kramer,

Third-Party Defendants.

Allen & Company and Allen & Company Incorporated,

Third-Party Counter-claimants,

-against-

Laventhol Krekstein Horwath & Horwath,

Third-Party Counterclaim Respondent-Appellant.

---

74 - 2405

CERTIFICATE OF SERVICE

The undersigned, a member of the Bar of this Court, hereby certifies that true copies of the Joint

Appendix - 5 Volumes have been duly served, by hand delivery on counsel for all parties who have appeared in the above actions, on the 23rd day of December, 1974.

BLUM HAIMOFF GERSON LIPSON & SZABAD, Esqs.
Attorneys for Plaintiff-Appellee
270 Madison Avenue
New York, New York 10016

POLLACK & SINGER
Attorneys for Third-Party Defendants-
Appellants
61 Broadway
New York, New York 10016

Jack David

Dated: December 24, 1974

Sir:

Take notice that the within is a copy of

which was duly made, entered and filed in the office of the Clerk of the

on the

day of 19

Dated, New York, N. Y. 19

Yours, etc.,

WILLKIE FARR & GALLAGHER

Attorneys for

Office and Post Office Address
1 Chase Manhattan Plaza
New York, N. Y. 10005

To:

Sir.

Take notice that the within

will be presented for settlement
at Term, Part
of the Court at the
Court House, in the
of , County of
on the day of
19 , at
o'clock M.
Dated New York, N. Y. , 19

Yours, etc.,

WILLKIE FARR & GALLAGHER

Attorneys for

Office and Post Office Address
1 Chase Manhattan Plaza
New York, N. Y. 10005

To:

UNITED STATES
FOR THE SECOND

Gerald L. Herz

Plaint

-against-

Laventhol Kreks

Defend

CERTIFICA

WILLKIE FA

ATTORNEYS FOR
1 CHASE M
NEW Y

Due and sufficie

is hereby admitted.
Dated New York, N

COURT OF APPEALS
CIRCUIT

Feld,

iff,

stein Horwath & Horwath,

dant-Appellant.

ATE OF SERVICE

RR & GALLAGHER
Plaintiff
MANHATTAN PLAZA
ORK, N. Y. 10005
422-3100

ent service of the within

N. Y. 19

Attorneys for